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THE SUPREME COURT'S ATTITUDE TOWARD LIBERTY OF CONTRACT AND FREEDOM OF SPEECH

A NEW JERSEY insurance agency succeeded in bringing to the Supreme Court of the United States its complaint that a New Jersey statute, prohibiting insurance companies from paying to any local agent commissions in excess of those paid to any other local agent, infringed upon its "liberty" to contract about its affairs in violation of the Fourteenth Amendment.[1] The complaint was appealing. Agency and principals had agreed upon a 25% commission as "reasonable" within the terms of their contracts. Both desired that the contracts be performed. The only obstacle was that another broker had agreed to accept a 20% commission. The latter made no complaint. Nothing stood in the way of performance of the contract, except the company's reluctance to disobey the statute. Four Justices of

[1] O'Gorman & Young, Inc. v. Hartford Ins. Co., 282 U. S. 251, 51 Sup. Ct. 130 (1931). This was a consolidation of two actions at law against two separate insurance companies to recover commissions alleged to be due under similar contracts with both. The companies pleaded the statute in defense.

the Court[2] recognized the obvious infringement of the parties' liberty, recalled the Court's prior insistence that "freedom of contract is the general rule, restraint the exception," and, having been given no grounds to justify the exception in the case before them, concluded, of necessity, that the statute was unconstitutional. But five Justices[3] took seriously what had hitherto come to be meaningless bromides, that the judicial annulment of legislative enactments is, at best, a dangerous business, that the power to that end is to be exercised only in the "clearest" cases, that statutes are not to be annulled unless invalidity is clearly proved by a presentation of the underlying facts which condition constitutionality. Since no "factual foundation of record for overthrowing the statute" was presented, and since it did "not appear upon the face of the statute, or from any facts of which the court must take judicial notice," that evils "did not exist" for which this statute was "an appropriate remedy" "the presumption of constitutionality" had, of necessity, to prevail.[4] The long list of cases cited by the four dissenters in which the "general rule" of liberty of contract was used to overthrow legislation even in the face of a factual foundation in favor of validity was simply ignored.

Less than one month after these opinions were read from the Bench, *Near v. Minnesota*[5] was argued before the same court. Near complained that a Minnesota statute which authorized a permanent injunction, issued by a Minnesota court, restraining him from publishing a newspaper containing "malicious, scandalous and defamatory matter" deprived him of "liberty" in violation of the Fourteenth Amendment. His complaint was not at all appealing. The nine issues of the newspaper which he had published prior to the injunction proceedings were part of the record in the case.[6] They were devoted in large part to scandalous charges against certain public officers of the county, private individuals, leading newspapers of the city, and the Jewish race. The articles were written in the vernacular

[2] Van Devanter, McReynolds, Sutherland and Butler, J. J.

[3] Hughes, C. J., Holmes, Brandeis, Stone and Roberts, J. J.

[4] In several later cases, attacks on legislation failed for similar lack of "factual foundation." See Notes (1931) 31 COL. L. REV. 1136, (1931) 40 YALE L. J. 657; Hamilton, *The Jurist's Art* (1931) 31 COL. L. REV. 1073.

[5] 283 U. S. 697, 51 Sup. Ct. 625 (1931).

[6] The suit for injunction was brought by the County Attorney pursuant to the authority conferred by the statute for the institution of such suit by him, or on his failure or refusal, by the Attorney General, or on his failure or refusal, by any citizen of the county. As interpreted by the State Court, the statute left all other civil and criminal remedies in force and was aimed not at the redress of private wrongs but at the suppression, for "the protection of the public welfare," of newspapers continually publishing scandalous and defamatory charges, with regard to private persons, or against public officers, of corruption, malfeasance in office or neglect of duty.

of the street, with bold-faced, large type generously interspersed for emphasis. The language was undoubtedly scurrilous. Style and language were obviously focused on appeals to prejudice and passion, even if truth were written. Near's associates in a prior enterprise of the same kind had concededly used that newspaper for blackmail purposes. Near made no attempt to prove the truth of any of his charges or that his "motives" were good.[7] He relied on his "freedom" to publish even false charges, conceding possible liability to subsequent punishment.

The Court again divided, exactly as in the *O'Gorman* case. Mr. Justice Butler, of Minnesota, wrote an opinion in which the three Justices who were with him in the *O'Gorman* case concurred. They agreed with the rest of the Court that "freedom of speech and of the press" was a "liberty" protected by the Fourteenth Amendment, but that it was nevertheless subject to some control by the State. The Minnesota courts had, "in due course of judicial procedure" adjudged that Near was engaged in the "business of publishing" "malicious, scandalous and defamatory matter" and abated it as a "public nuisance." The statute authorizing this measure was passed "in the exertion of the State's power of police" and the Supreme Court, "by well established rule," must assume "until the contrary is clearly made to appear, that there exists in Minnesota a state of affairs that justifies this measure for the preservation of the peace and good order of the State." And they pointed, *inter alia,* to chapter and verse in the *O'Gorman* case. Not only did Near's attack lack "factual foundation," but the presumption of validity was bolstered by the obvious scurrility of the articles, by the history of Near's previous enterprise, by the shootings which Near himself attributed to his publications.

The five Justices, whose teaching in the *O'Gorman* case had thus been absorbed, were willing to accede to these characterizations of Near's business and publications. They were willing to assume the falsity of his charges,—to admit that the persons involved in them were "impeccable." But they found in the "general conception" of "liberty of the press, historically considered and taken up by the Federal Constitution," the "essential attribute" of freedom from "previous restraint" which they thought was violated by the statute. While recognizing as "undoubtedly true" that "the protection even as to previous restraint is not absolutely unlimited," the limitations were of such "exceptional nature" as only to clarify the "general conception" and were "not applicable" to the case at bar. Charges

[7] The statute made "available the defense that the truth was published with good motives and for justifiable ends." Whether the same defense would be available in contempt proceedings for violation of the injunction was left in doubt both by the statute and by the State Court.

like those made by Near "unquestionably create a public scandal, but the theory of the constitutional guaranty is that even a more serious public evil would be caused by authority to prevent publication." That the liberty of the press may be abused by "miscreant purveyors of scandal" does not lessen the necessity of immunity of the press from previous restraint "when dealing with official misconduct," even as the existence of abuses in "the wide field of activity in the making of contracts," which is otherwise "subject to legislative supervision," had been held by the Court to be insufficient to justify interference "with what are deemed to be certain indispensable requirements" of the "liberty of contract," "notably with respect to the fixing of prices and wages." The *O'Gorman* case, and the reliance on it by the minority, was not mentioned. The statute was declared invalid and the decree granting the injunction reversed.

Thus was the conflict between the two groups thrown into sharp relief. Every member of the Court changed his attitude, shifting from one rule of presumption in the one case to an opposite rule of presumption in the other. But the two cases do more than illustrate the opportunistic use of precedents and logic. They do more than distinguish the five Justices who constituted the majority in both. They are a hopeful sign pointing in the direction of the ideal of freedom.

The ideal of freedom, has been termed "the holy grail of social progress." [8] The way to its acquisition may be blocked by the tyranny of government. But governmental restraints are not the sole obstruction. The path may be blocked even more effectively by physical barriers, or by our whole complex social and economic organization. Even in the absence of governmental restraint, one is not free to grow plants in rock; nor is a miner free to join a union when the cost is loss of his job and inability to secure another. Our state and federal governments have attempted, therefore, to secure greater freedom to individuals by compelling the removal of compulsions incident to our social and economic organization, by limiting the power of some to dominate the choice of others. Such attempts were the minimum wage laws, the hours of labor laws, the yellow dog contract, employment agencies and ticket-scalping legislation. When the constitutionality of this legislation was challenged, the Supreme Court postulated the existence and maintenance of the economic organization in which we happened to find ourselves. When it invalidated these statutes in the name of "liberty" protected by the Fourteenth Amendment, it frankly meant the liberty to maintain, promote and exploit advantages

[8] Hamilton, *"Freedom and Economic Necessity,"* in KALLEN, FREEDOM IN THE MODERN WORLD (1928) 25.

which some had secured as a result of that organization.[9] The "liberty" protected was liberty from governmental attempts to relax human, economic constraints on freedom. Of course, that protection had not always been accorded. The full potentialities of the due process clauses in this regard were slow in being recognized.[10] But after recognition, the clauses became a bar to be hurdled only by legislation supported by a strong showing of appropriateness under the "police power." The presumption of constitutional validity always received a verbal bow; the real embraces were given the presumption of constitutional invalidity.

The change in the Court's affections, displayed by the majority in the *O'Gorman* case, can undoubtedly be justified simply by the ugly appearance of the record. The case was confessedly a test suit. Yet, no party interested in upholding the statute was joined or appeared. The respondents, like the petitioner, were willing, perhaps even anxious, to have the statute invalidated. The issues had been joined by motions to dismiss the defendants' answers based on the statute. Apparently no evidence was offered or introduced at the hearing on the motions. The record before the Supreme Court comprised but forty-two pages and consisted wholly of the formal pleadings in the two cases, captions, formal notices between counsel and the formal papers on appeal. Not a line in the record added anything to the words of the statute by way of light for the determination of the issue of constitutionality. While the petitioner in the Supreme Court filed a thirty-nine page brief in opposition to the act, in addition to the "statement as to jurisdiction on appeal," a single attorney filed but one four page brief for both insurance companies in its defense. He cited four cases and filled two pages of the brief with quotations of general statements from them.[11] Even if the fate of this legis-

[9] See Pitney, J. in Coppage v. Kansas, 236 U. S. 1, 17, 35 Sup. Ct. 240, 244 (1915): "No doubt, wherever the right of private property exists, there must and will be inequalities of fortune; and thus it naturally happens that parties negotiating about a contract are not equally unhampered by circumstances."

[10] See Warren, *The New "Liberty" Under the Fourteenth Amendment*, (1926) 39 HARV. L. REV. 431, 422 *et seq.*

[11] After argument, pursuant to the Court's permission, he filed "supplemental memoranda" of three and one-half pages in which he set forth for the first time somewhat similar legislation of Missisippi and Louisiana relating to commissions of insurance agencies. He had also "gathered from questions addressed by members of the Court that doubt was entertained as to the good faith of the defendants. . . . in defending the statute" and he attempted to quiet the doubt. While the companies were willing to pay the petitioners the commissions agreed upon, if the statute did not prohibit, they were "desirous of final determination as to [its] constitutionality." The particular "form by which the constitutionality was being tested" was chosen, in preference to suit for injunction against the state officers, not in

lation were ordinarily to be settled by a struggle with the presumption of invalidity, pure sportsmanship could hardly permit the award of victory to the presumption when the statute's cause was championed by a straw gladiator.[12] But the majority's opinion shows more than sportsmanship. Recent developments have indicated that our economic organization has not the skill of conveniently curing its ills. Governmental aid appears inevitable. Man is not born into our society free of economic constraints. Legislation relaxing them may more likely be an enhancement of than a restriction upon the "liberty of contract." The Court is not to stand in the way of experimentation. The addition of two vigorous thinkers to the Bench has carried the day for pragmatism and liberal tolerance of legislative experiment with control for the purpose of advancing a larger capacity for individual freedom.

Personal liberties, freedom of speech and of the press, received constitutional protection earlier than the "liberty of contract," but the protecting cloak of the Fourteenth Amendment was not thrown over them till after that liberty had become firmly established.[13] The Federal Constitution contains in the First Amendment the absolute prohibition that "Congress shall make no law . . . abridging the freedom of speech, or of the press." The state constitutions generally qualify the similar prohibition on state legislatures with a clause saving power to impose responsibility for abuse of the freedom thus guaranteed. But the difference in phraseology is apparently nothing more than that. Judicial interpretation has engrafted even on the absolute prohibition a limitation in favor of a power "inherent" in government to protect itself and to maintain "peace and order." After the abortive Alien and Sedition Laws of 1798, Congress has not directly restrained freedom of speech and of the press until the Espionage Acts of the World War period. Long prior to the war, however, the states had imposed restraints and the patriotic fervor of the war brought on a further avalanche.[14]

The Espionage Acts survived attack based on the First Amend-

bad faith, but simply to avoid procedural difficulties in the New Jersey practice which might have hindered "decision on the real question in issue." The parties' unusual preferment of the state courts over the federal district court, in which this test suit could have been prosecuted either originally or by removal, apparently needed no explanation, although federal jurisdiction existed both on federal question and diversity of citizenship grounds. In conclusion, counsel expressed the belief "that every case that can throw light on the subject has been presented to this court."

[12] A test case staged like the O'Gorman case involves even greater evils than those feared from advisory opinions and declaratory judgments. See Frankfurter, *Note on Advisory Opinions* (1924) 37 HARV. L. REV. 970.

[13] See Warren, op. cit. *supra* note 10.

[14] See CHAFEE, FREEDOM OF SPEECH (1920) c. 1 and 4.

ment, but with the important qualification, laid down for a unanimous court by Mr. Justice Holmes, that "the question in every case is whether the words used are used in such circumstances and are of such a nature as to create a clear and present danger that they will bring about the substantive evils that Congress has a right to prevent." The Court assumed that the prohibition of laws abridging the freedom of speech was "not confined to previous restraints, although to prevent them may have been the main purpose." [15] With one possible exception,[16] state restraints, until the last term, met with similar success. The battle was waged on the front of the "privileges and immunities" and "due process" clauses of the Fourteenth Amendment. The statutes imposed punishment for talk not censorship. The Court "assumed" for the purposes of the cases before them that freedom of speech was a "liberty" and that the due process clause limited the power to punish as well as the power to impose previous restraint.[17] It found that the restraints imposed were within "implied exceptions" to the prohibition.[18]

In *Stromberg v. California* [19] and *Near v. Minnesota,* the Court

[15] Schenk v. United States, 249 U. S. 47, 52, 39 Sup. Ct. 247, 249 (1919). See Note (1931) 31 COL. L. REV. 1148 and CHAFEE, op. cit. *supra.* note 14, for sources as to freedom of speech and previous restraint.

[16] Fiske v. Kansas, 274 U. S. 380, 47 Sup. Ct. 655 (1927).

[17] Gitlow v. New York, 268 U. S. 652, 666, 45 Sup. Ct. 625, 630 (1925). As late as 1922, in answering a contention that freedom of speech included a "freedom of silence," which was infringed by a state statute requiring employers to give "service letters" to discharged employees, the Court said that "neither the Fourteenth Amendment nor any other provision of the Constitution of the United States imposes upon the States any restriction about 'freedom of speech'." Prudential Ins. Co. v. Cheek, 259 U. S. 530, 543, 42 Sup. Ct. 516, 522 (1922).

[18] But in reviewing cases under state acts, the Court was not to be governed by the considerations announced in the Espionage cases. Those were deemed to refer only to the interpretation of the Espionage Acts—not to the issue of constitutionality. In reviewing cases from state courts, the Court was not to consider whether "in each case" the words were spoken under "such circumstances" and were "of such a nature" as to create "a clear and present danger" that they would bring about the "substantive evils" that the states have "a right to prevent." It was to consider only whether the legislature could have determined reasonably that the "class" of language prohibited by the statute, as verbally interpreted, rather than as effectively administered, created a reasonable danger of such substantive evils. And of this, the mere enactment of the statute would be weighty proof. Gitlow v. New York, 268 U. S. 652, 670, 45 Sup. Ct. 625, 631 (1925). But compare Brandeis' dissent in Whitney v. California, 274 U. S. 357, 372, 374, 47 Sup. Ct. 641, 647 (1927), and the last paragraph of the Court's opinion in the Stromberg case, *infra* note 19.

[19] 283 U. S. 359, 51 Sup. Ct. 532 (1931). The Court declared invalid the provision in the California Penal Code making it a felony to display a red flag "as a sign . . . of opposition to organized government." Since Miss Stromberg's conviction might have been based on that provision alone, the Court found it unnecessary to pass upon the provisions making felonious the

held affirmatively, rather than assumed *ad hoc*, that freedom of speech was a "liberty" within the due process clause. In both cases, the plaintiff's interests could well have been regarded as interests of substance, of "property", just as in *Meyer v. Nebraska*[20] and *Pierce v. Society of Sisters*[21] freedom to teach was referred to the teacher's calling and to the school's business—"property-liberty" protected by the Fourteenth Amendment. Instead, the legislation was invalidated on the ground that "liberty" was taken without due process. Personal liberty. Liberty without material value. In authorizing an injunction with the power to punish for contempt, the statute in the *Near* case was deemed to impose a censorship by the equity court—a *previous* restraint on speech. The statute was therefore declared invalid, not because restraint was unjustified but because the form in which it was to be exerted was not permissible.

The difference between previous restraint and subsequent punishment does not, of course, determine the effectiveness of the restraint. As has been suggested, a death penalty for publication would be a more effective preventive than censorship. The injunction issued in the *Near* case was phrased in the exact words of the statute. It was no more definite or vague in its prohibitions than was the statute. If the statute had provided only for criminal punishment for the proscribed publications, Near would have been under exactly the same restraint arising from the statute itself as he was under the injunction. With one difference. A violation of the supposed statute would have resulted in a criminal prosecution before a judge and probably also a jury. A violation of the injunction would have resulted in summary contempt proceedings before the equity judge. The difference is striking in view of the historic struggle for greater jury powers in criminal libel cases.[22] But it wanes considerably in view of the Supreme Court's holding that the Federal Constitution contains no guaranty of jury trial in state courts.[23] It would

display of a flag as "an invitation or stimulus to anarchistic action or as an aid to propaganda that is of a seditious character." It did not have "to review the historic controversy with respect to 'sedition laws' or to consider the question as to the validity of a statute dealing broadly and vaguely with what is termed seditious conduct, without any limiting interpretation either by the statute itself or by judicial construction." *Cf.* the opinion of Brandeis, J. in the Whitney case, *supra* note 18. The death gasp of the doubt as to whether "liberty" in the Fourteenth Amendment includes freedom of speed and of the press is uttered in the dissenting opinion of Mr. Justice Butler in the Stromberg case.

[20] 262 U. S. 390, 43 Sup. Ct. 625 (1923).

[21] 268 U. S. 510, 45 Sup. Ct. 571 (1925).

[22] See CHAFEE, *op. cit. supra* note 14, c. 1; Pound, *Equitable Relief Against Defamation* (1916) 29 HARV. L. REV. 640, 655.

[23] See Note (1931) 31 COL. L. REV. 468. The doubt as to whether truth

have been more gratifying if the inarticulate dislike of legislation which imposes so vague and so dangerous a restraint upon freedom of speech had been made articulate.

But, by whatever means, the Court has removed an obstruction to freedom of speech and of the press. Only commendation can be given to the majority's refusal to yield to the importunities of the minority in the *Stromberg* and *Near* cases, that procedural difficulties and technical faults in the conduct of the litigation below prevented consideration of the larger issues on which the decisions were based. Review by the Supreme Court, even if its members were of one mind, is a weak safeguard of personal liberty. It can review only a very small fraction of the cases litigated. For the most part, this liberty is at the mercy of executive and administrative officers and trial courts. But while personal liberty must thus look for protection to our generally becoming "more civilized," the Supreme Court can set a brilliant example.[24]

The existing capacities for freedom of speech and of the press, its impingement on the liberty of others and the incidence of the legislation thereon differ widely from that of the freedom of contract sought to be protected against hours of labor, minimum wage, "yellow dog contract", and similar laws. "Freedom to think as you will and to speak as you think" is the vehicle to more general liberty; its complete exercise by some does not infringe upon the like liberty of others, whatever other evils it may

would be a defense in contempt proceedings should be mentioned as a further possible difference.

[24] Innumerable restraints on freedom of thought and speech exist with only the remotest, if any, possibility of Supreme Court review: in the enforcement of laws relating to immigration, naturalization, deportation, the mails (*cf.* Milwaukee Pub. Co. v. Burleson, 255 U. S. 407, 41 Sup. Ct. 352 (1921)) the tariff, radio broadcasting, the theatre, public assembly, street speaking and all manner of local police ordinances with avowed objects such as facilitation of traffic, *etc.* See Comment (1931) 40 YALE L. J. 967; Note (1931) 31 COL. L. REV. 1148; Grant and Angoff, *Massachusetts and Censorship* (1930) 10 BOSTON U. L. REV. 36, 147. Mr. Justice Butler's attempt in the Near case to assimilate scandalous charges against public officers with "obscene" publications overlooks obvious differences, as would also an assimilation of such charges, and of discussions of political, social or economic problems, with invasions of privacy by the publication of matters concerning only an individual's private affairs and having no public interest other than the satisfaction of curiosity. Compare the English equity jurisdiction to restrain publication of certain libels on candidates for public office on the eve of an election, DAWSON, LAW OF THE PRESS (1927) 197.

The serious abridgments of freedom of speech and other personal liberties by labor injunctions issued for the avowed purpose of protecting private property, without regard to the public interest involved, cries for courageous action. See the dissenting opinion of Judge Maxey in Kraemer Hosiery Co. v. Schmidt, Supreme Court of Pennsylvania, Oct. 9, 1931.

cause. But freedom to contract as you will and impose whatever conditions you can may be a sure means of oppression; its complete exercise by some often results in the curtailment of the like freedom of others. A larger capacity for liberty to contract in our economic organization may well need governmental control of the power to exert economic compulsion.[25] But a larger capacity for the liberty of speech needs primarily absence of governmental restraint on speech. Legislation designed to promote a larger capacity for freedom by the relaxation of economic compulsion may, indeed, be presumed valid. But a contrary presumption seems eminently proper when legislation constricts the existing larger capacity by imposing new governmental restraints.

H. S.

SIXTH TENTATIVE DRAFT OF A UNIFORM MECHANICS' LIEN STATUTE

MECHANICS' lien acts, designed primarily to protect one who contributes his services to the improvement of real property by constituting it a security for his remuneration, require delicate draftsmanship in order to accomplish this purpose without infringing upon rights of the owner of the property and third parties whose interest in it may be affected by such liens. The effectiveness of the tentative draft of a Uniform Mechanics' Lien Act,[1] recently approved by the National Conference of Commissioners on Uniform State Laws, in achieving a fair balance between these conflicting interests can best be estimated by comparison with present statutes.

State statutes very generally stipulate that the right given the lienor is one *in rem*,[2] and that the liability of the owner's property is measured by the price stated in his original contract with the general contractor.[3] Both of these provisions are adopted by the Uniform Act in section 2. Further, it is customarily provided

[25] The very rapid growth of the use of standardized contracts (see Comment (1931) 40 YALE L. J. 640, 644) is only one of the striking indications that in reality the issue, in the economic world, is not as to a choice between complete individual freedom and governmental control, but rather as to a choice between governmental control and existing control by other institutions.

[1] Report of Committee on Uniform Mechanics' Lien Act, including Sixth Tentative Draft of a Proposed Act, National Conference of Commissioners on Uniform State Laws, Sept. 8-14, 1931.

[2] See for example COLO. STAT. ANN. (Courtright's Mills, 1930) § 4580; R. I. GEN. LAWS (1923) c. 301-1. But *cf.* VA. CODE ANN. (1930) § 6426a (owner made personally liable to the extent of his indebtedness to the contractor at the time notice is given).

[3] KY. STAT. (Carroll, 1930) § 2463; MICH. COMP. LAWS (1929) § 13101.

that when one entitled to a lien notifies the owner of the existence of an unpaid debt for services owed him by the contractor, the owner shall withhold such sum from his payments during the progress of the work, for the benefit of the lien claimant.[4] But they fail to specify to any sufficient degree what payments by the owner to the contractor or lienors, actually operate to reduce his statutory liability to other lienors. Where the amount recovered by lienors against the owner's property is greater than the contract price less installments already paid to the general contractor, several states allow the owner to recover the excess;[5] but a right of action against a probably insolvent contractor is only a doubtful protection. A few states provide that while the property shall not become liable for more than the original contract price, the owner must assume the risk of all payments made within the time allowed a lienor for filing his claim of lien, usually a specified number of days after the lienor performs the last labor or last furnishes materials.[6] So general a provision is also unsatisfactory, not only to the owner, who will hesitate before making any payment, but also to the contractor who depends on the regular installments of the agreed price. A third, rare type of provision fixes the terms of the original contract without regard to the desires of the parties by requiring the postponement of certain payments for a specified period.[7] Such a provision,

A few statutes increase the owner's liability. ALA. CODE ANN. (1928) § 8832 (materialmen become entitled to full value of claim by giving early notice to owner who does not repudiate such liability); ARIZ. REV. CODE (Struckmeyer, 1928) § 2020 (owner liable for reasonable value of labor or materials furnished his agent); CAL. CODE OF CIV. PROC. (Deering, 1923) § 1183 (liens limited to contract price only if bond filed); ILL. REV. STAT. (Smith-Hurd, 1929) c. 82, § 22-25 (property may become liable for full debt on notice to owner); IOWA CODE (1931) § 10280 (only one class of liens limited to amount due contractor from owner); MISS. ANN. CODE (1930) § 2274 (owner loses limited liability by denying any indebtedness due contractor, in foreclosure suit by lienor).

[4] See N. Y. CONS. LAWS (Cahill, 1930) c. 34, § 14; N. C. CODE ANN. (1927) § 2439.

[5] See IDAHO COMP. STAT. (1919) § 7350. Alabama, Arizona, Arkansas, California, New Mexico, Nevada and Oregon have similar statutes. *Cf.* TEX. COMPL. STAT. (1928) § 5463.

[6] KAN. REV. STAT. ANN. (1923) c. 60 § 1403. *Cf.* OHIO GEN. CODE (Page, 1926) § 8312 (risk on owner for stated period if he pays without requiring a statement as to sums due lienors from contractor). These statutes leave it uncertain whether at any given time the risk is upon the owner in favor of all lienors until the expiration of the period within which the last lien claimant could file his statement, or whether the risk exists only as to those whose periods have run.

[7] COLO. STAT. ANN. (Courtright's Mills, 1930) § 4581 (no advance payments on contract to be made; at least 15% of contract price to be payable no sooner than thirty-five days after complete performance of contract; no payments prior to that time will defeat or diminish the lienor's claim);

while not objectionable to the owner, may be decidedly disadvantageous for the contractor. By far the most prevalent type of provision declares that the liability of the owner to any lienor, in respect to his property, is limited to the contract price less payments in good faith to the contractor.[8]

In adopting the underlying theory of this last provision, the Uniform Act has attempted to remedy its failure to define "payments in good faith" by a well organized, novel summary on the subject of "money properly paid." The owner may at any time pay a laborer the amount due him for his services to the property.[9] All liens, except those of laborers or persons contracting directly with the owner must be perfected by notice, and lienors who give such notice within a limited time are preferred to those who are not so diligent.[10] The owner may pay a preferred lienor any amount owed him, provided that the balance of the contract price, after all other proper payments are deducted, is sufficient to pay all other preferred lienors and laborers the amounts due or to become due them.[11] But payments to other lienors are not "properly" made unless a sufficient amount remains, after all proper deductions, to pay all debts due or to become due to laborers, including those subsequently employed, and to all lienors who have previously given or thereafter give notice.[12] When the contract price is insufficient for payments in full the owner may pay any lien claimant the pro-rata amount for which his claim would ultimately be allowed.[13] Payments to the general contractor (which are *prima facie* made in good faith) are properly made when due and payable according to the original contract, providing that after all proper deductions a sum remains, out of the contract price, sufficient to pay all laborers and all other lienors who have previously given, or thereafter give, notice.[14]

However, the added clarification of the owner's position with regard to payments made during the progress of the work is accompanied by an unprecedented increase in his risk. Since laborers are not required to give any notice, he must discover at his peril all sums due or to become due them, with the further

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ORE. CODE ANN. (1930) c. 51-110; *cf.* W. Va. OFFICIAL CODE (1931) c. 38-23 (owner must require bond from contractor under penalty of subjecting his property to a liability to the full extent of all claims).

[8] See CONN. GEN. STAT. (1930) § 5108; N. Y. CONS. LAWS (Cahill, 1930) c. 34, § 4.

[9] UNIFORM MECHANIC'S LIEN ACT, § 5-2.

[10] *Ibid.* § 4.

[11] *Ibid.* § 5-3.

[12] *Ibid.* § 5-4.

[13] *Ibid.* § 5-5.

[14] *Ibid.* § 5-8. For statutes making special concessions to laborers concerning notice, see IND. STAT. ANN. (Burns, 1926) § 9831; MICH. COMP. LAWS (1929) § 13101; WIS. STAT. (1929) § 289.02(2).

disadvantage that progress payments or payments direct to lienors do not lessen the liability of his property to laborers subsequently employed. Yet an owner of real property would probably be better able to bear a financial loss than a laborer,[15] though the same cannot be said with any degree of certainty of materialmen, subcontractors or skilled specialists. The owner can always, however, distribute the risk by requiring a bond from the contractor conditioned on full and faithful performance including payment of all lien claims.[16] Nor does the Uniform Act leave him without safeguards in the matter of payment, since it gives him the right to demand from the lienor, whenever any payment is due the contractor, a written statement under oath concerning his account with the contractor,[17] and the further right to require the contractor before the final payment to furnish a similar itemized statement as to his accounts with all lienors,[18] upon which the owner may in good faith rely, except as regards the liens of laborers. The furnishing of a false statement to the owner with intent to defraud is made a crime.[19]

The Uniform Act does not expressly state whether the owner in a suit by employees of the contractor to foreclose a lien, may set-off or counterclaim for damages based upon the contractor's failure to perform.[20] Some state statutes have given,[21] and a few have denied [22] the right, and consequently judicial holdings under

[15] Laborer is defined by the Uniform Act, Section 1, as "any person other than an architect, landscape architect, engineer and the like, who, under properly authorized contract, personally performs on the site of the improvement labor or services for improving real property."

[16] *Ibid.* § 7.

[17] *Ibid.* § 26-2.

[18] *Ibid.* § 4-3, and 5-12. The present Ohio statute provides that the risk of payment within a specified period is on the owner unless before each payment an itemized statement of the contractor's accounts with all his employees is required, accompanied by a similar itemized statement of all subcontractors, and certificates of all materialmen. In making payments the owner may rely upon these to reduce the liability of his property. OHIO GEN. CODE (Page, 1926) § 8312. Under such a statute the risk as to amounts to become due in the future rests upon the lienors. The Uniform Act seems preferable in that, as has been pointed out, the owner can better bear such risk. And his right to demand a statement from any lienor at the time of payment seems to protect him as to the claims presently existing as fully as the more cumbersome Ohio procedure.

[19] UNIFORM MECHANICS' LIEN ACT, § 9.

[20] § 2 gives a lien for services furnished in accordance with the claimant's contract and the direct contract. Therefore the right of set-off or counterclaim may possibly be implied against such lienors.

[21] D. C. CODE (1929) § 354; MICH. COMP. LAWS (1929) § 13101; N. C. CODE ANN. (1927) § 2476; OHIO GEN. CODE (Page, 1926) § 8313; *cf.* VA. CODE ANN. (1930) § 6483.

[22] COLO. STAT. ANN. (Courtright's Mills, 1930) § 4581; CAL. CODE OF CIV. PROC. (Deering, 1923) § 1200 (repealing a former provision allowing the right).

a statute without express provision in the matter will probably vary, thus defeating the purpose of a uniform act. A definite provision might well have been inserted. Likewise there has been division among the states as to whether an owner may stipulate in a building contract that his property shall not be subject to the liens of an employee of the contractor.[23] Since such a stipulation nullifies the effect of a mechanics' lien act, it should be expressly forbidden by the Uniform Act to prevent a judicial decision upholding the contract.

The provisions of the Uniform Act with regard to the rights of lienors are significant in two particulars, namely the priorities among lienholders, and the protection given the individual against encroachments on his rights by fellow lienors. With respect to the latter, the provisions in Section 5 of the Uniform Act are unique in the protection afforded lienors against loss through payments to fellow lienors, as discussed above. As to priority, however, practically all the states have legislated. Many provide that, except for the general contractor's lien, there shall be an equal right in the property to the extent of its liability.[24] Others divide lienors into classes, each of which is to be paid in full, or, if the amount available is not sufficient, pro-rata, before any other class shall be entitled to payment. Of these latter, some base priority on the time of giving or filing notice.[25] A rare basis of classification has been the order in which the work was done or the materials furnished.[26] The more approved practice, however, has been to give priority to the liens of laborers as a class, thus giving the greatest protection where it is most needed.[27] The Uniform Act creates classes having priority in the following order (a) liens of laborers; (b) liens of all other lienors who have given notice of an intention to claim a lien within a limited period after their services were first rendered; (c) all other liens except that of the contractor; (d) the contractor's lien.[28]

This differentiation between lienors on the basis of whether or not notice was given within a stated period after the lienor be-

[23] For states allowing such stipulations upon the filing of the contract among public records, see ILL. REV. STAT. (Smith-Hurd, 1929) c. 82, § 21; IND. STAT. ANN. (Burns, 1926) § 9831; PA. STAT. ANN. (Purdon, 1930) Title 49, § 72; *cf.* MAINE REV. STAT. (1930) c. 165 § 30. For statutes nullifying such stipulations see CAL. CODE OF CIV. PROC. (Deering, 1923) § 1201; WIS. STAT. (1929) § 289.03; COLO. STAT. ANN. (Courtright's Mills, 1930) § 4600; *cf.* N. Y. CONS. LAWS (Cahill, 1930) c. 34 § 34. *Cf.* UNIFORM MECHANICS' LIEN ACT, § 27.

[24] See ARIZ. REV. CODE (Struckmeyer, 1928) § 2036; MICH. COMP. LAWS (1929) § 13109; *cf.* D. C. CODE (1929) § 362.

[25] FLA. GEN. LAWS (Skillman, 1927) § 5379; IOWA CODE (1931) § 10286.

[26] DEL. REV. CODE (1915) § 2850.

[27] ILL. REV. CODE (Smith-Hurd, 1929) c. 82, § 27; N. Y. CONS. LAWS (Cahill, 1930) c. 34, § 25.

[28] UNIFORM MECHANICS' LIEN ACT § 6.

gan to render services, seems desirable. It is not open to the objection which obtains when priority because of notice follows strictly on the order of giving notice, namely, that it is unfair to lienors who begin work at a late date.[29] Nor does it create an incentive to hasty filing of lien claims, inevitably prejudicial to the credit of owner and contractor,[30] since the priority is based on a written notice to the owner within the given period, and not on the time of filing. On the contrary the provision works a definite benefit to the owner, whose risk as to payments is so great under the Uniform Act, since it will lead to immediate disclosure to him of any unpaid accounts. Since the differentiation will probably cause immediate disclosure in almost all cases, the practical effect of this provision would seem to confer the same status upon all lienors other than the laborer and contractor.

The contractor, unlike other lienors, receives less protection in the Uniform Act than is now afforded him by many state statutes. The provision allowing early filing of liens [31] may seriously injure his credit,[32] while serving no useful purpose to lienors since it is also provided that liens relate back to the time of the visible commencement of operations,[33] and are prior to all other encumbrances on the real estate subsequently recorded.[34] Certain state statutes now provide that claims of liens may not be filed until the lienor has fully performed his services,[35] or even for a given period after that time.[36] It is to be regretted that the Uniform Act does not contain a similar provision for the contractor's protection. It does, however, protect him against vexatious claims of lien by penalizing the claimant,[37] although the penalty is less severe than that provided for by most state statutes.[38]

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[29] Current Legislation (1929) 29 COL. L. REV. 997, 1003.

[30] Current Legislation (1930) 5 ST. JOHN'S L. REV. 152, 155.

[31] By section 17 of the Uniform Act claims of liens may be filed at any time during the progress of the work, but not later than three months after the completion of the lienor's services.

[32] Current Legislation (1930) 5 ST. JOHN'S L. REV. 152, 155.

[33] UNIFORM MECHANICS' LIEN ACT § 3-1.

[34] *Ibid.* § 21.

[35] See FLA. GEN. LAWS (Skillman, 1927) § 5380 (2).

[36] See DEL. REV. CODE (1915) § 2850. (twenty days after completion of services); *cf.* MO. REV. STAT. (1929) § 3175 (lien cannot be filed until ten days after notice to owner); CAL. CODE OF CIV. PROC. (Deering, 1923) § 1184a (suits may not be brought until expiration of filing period).

[37] UNIFORM MECHANICS' LIEN ACT § 26-2 (lienor furnishing false statement deprived of lien to extent he has prejudiced an interested party's right).

[38] *Cf.* ARK. DIG. STAT. (Crawford & Moses, 1921) § 6921 (failure or refusal to furnish correct list constitutes misdemeanor); CAL. CODE OF CIV. PROC. (Deering, 1923) § 1202 (forfeiture made penalty for wilfully giving false notice of lien); N. Y. CONS. LAWS (Cahill, 1930) c. 34, § 39a (damages to owner where lien wilfully exaggerated).

A substantial part of the difficulties in mechanics' lien law has risen from the issue of priority as between lienors and other encumbrancers. Present statutes generally provide that mortgages or other encumbrances on land recorded prior to the creation of a particular mechanic's lien, whether its existence date from the time of filing the lien,[39] the time when the lienor's services were performed,[40] the time of serving notice on the owner,[41] or from the visible commencement of building operations,[42] shall be superior to that lien as to the land. Under the first three conditions a mortgage recorded during the process of improving the land may at once have priority over some liens, and be subordinate as to others, thus creating priority classes among lienors never contemplated by the statute.[43] The Uniform Act successfully avoids this difficulty, by providing that liens shall relate back to the visible commencement of building operations.[44] But the Act fails to remedy in express terms a further defect of many state acts, namely, their failure to allocate the risk of loss between a mortgagee of land upon which there is a building at the time of the mortgage, and lienors who have merely altered or repaired such building. Existing statutes generally declare a lien on buildings to be prior to a previously recorded mortgage on *land* without specific provision for the repair situation.[45] The

[39] CONN. GEN. STAT. (1930) § 5105; KY. STAT. (Carroll, 1930) § 2463; MASS. GEN. LAWS (1921) c. 254, § 7; N. J. COMP. STAT. (Cum. Supp., 1925) c. 126-15; S. C. CODE OF LAWS (1922) § 5669; *cf.* MISS. CODE ANN. (1930) § 2258; *cf.* N. Y. CONS. LAWS (Cahill, 1930) c. 34, § 13(1).

[40] ARK. DIG. STAT. (Crawford & Moses, 1921) § 6922; CAL. CODE OF CIV. PROC. (Deering, 1923) § 1186; N. M. STAT. ANN. (1929) c. 82-205; OKLA. SESS. LAWS (1923) c. 54 amending OKLA. COMP. STAT. ANN. (1921) § 7461; WASH. COMP. STAT. (Remington, 1922) § 1132; W. VA. OFFICIAL CODE (1931) c. 38, § 17.

[41] FLA. GEN. LAWS (Skillman, 1927) § 5381 (1).

[42] MICH. COMP. LAWS (1929) § 13109; MO. REV. STAT. (1929) § 3163; NEV. COMP. LAWS (Hillyer, 1929) § 3738; *cf.* MINN. STAT. (Mason, 1927) § 8494.

[43] Comment (1926) 36 YALE L. J. 129, 132.

[44] UNIFORM MECHANICS' LIEN ACT § 3-1. § 21 avoids any question which might have arisen as to the priority of a previous unrecorded mortgage by providing that mechanics' liens shall be prior to "a conveyance, mortgage, building loan contract, attachment, judgment or other incumbrance against such real property which was not recorded, docketed, or filed at the time of the visible commencement of operations."

[45] ARK. DIG. STAT. (Crawford & Moses, 1921) § 6922; TEX. COMPL. STAT. (1928) § 5459; *cf.* PA. STAT. ANN. (Purdon, 1930) title 49, § 26 (material change constitutes "new" structure); but *cf.* statutes expressly providing for the repair question: VA. CODE ANN. (1930) § 6436 (encumbrance on both land and buildings previous to lien has priority over lien); ILL. REV. STAT. (Smith-Hurd, 1929) c. 82, § 2 lienor has priority as to enhanced value of property); TENN. ANN. CODE (Shannon, 1917) § 3536 (mortgagee's prior lien subordinate if, after learning of the improvement, he fails to give the lienor notice to the contrary); LA. REV. STAT. ANN.

Uniform Act declares that liens provided by the act shall have priority over encumbrances against such "real property" not filed at the time of the visible commencement of operations.[46] Section 1 defines "real property" as "the land that is improved and the improvements thereon, including fixtures . . ." Consequently, although the result is not a necessary one, it may be implied that incumbrances on both land and buildings actually recorded before the work begins will be prior to liens for repairs.[47]

Further problems are presented by mortgages given under building loan contracts by which the mortgagor-owner receives his loans in installments. Since the building is not yet in existence, the lender who contracts with an unscrupulous or negligent owner may find his security subject to the liens of laborers.[48] Statutory attempts have been made to meet the problem by giving complete priority to the building-loan mortgage,[49] or by preferring it only to the extent of advances made before the filing of the lien.[50] Under the latter provision, however, the number of priority classes created among lienors would be limited in number only by the number of installments provided for in the building loan contract. A more desirable type of provision now incorporated in the New Jersey [51] New York [52] and Ohio [53] statutes gives priority to the building loan mortgage, but insures that installments under it shall be first applied to the claims of lienors. The Uniform Act by section 8-2 makes it a crime for an owner, with intent to defraud, to apply the net proceeds of such a loan to any other purpose than to pay for labor or materials furnished on such improvement. Although the result is to minimize any conflict between the lender and the lienor, it might have been better achieved by incorporating in addition the New York, New Jersey and Ohio provisions, making the mortgagee's priority de-

(Marr, 1926) Act. 139 of 1922, § 8 (those having mechanics' liens have priority over such encumbrances, except that of vendor previously recorded, whenever made). It has been held that in the absence of a statute expressly giving mechanics' liens priority as to buildings erected subsequent to the recordation of a mortgage on land, the vested right of the mortgagee attaches to the land and whatever may become an integral part thereof. Leach v. Minick, 106 Iowa 437, 76 N. W. 751 (1898); see Note (1927) 15 GEO. L. J. 477.

[46] UNIFORM MECHANICS' LIEN ACT, § 21.

[47] For a general discussion of the problem, and the conflicting case law which has developed on the subject in the absence of an express statute on the subject, see Comment (1926) 36 YALE L. J. 129; Note (1927) 15 GEO. L. J. 477.

[48] Current Legislation (1929) 29 COL. L. REV. 996.

[49] See ARK. DIG. STAT. (Crawford & Moses, 1921) § 6909.

[50] D. C. CODE, ANN. (1929) § 359.

[51] N. J. COMP. STAT. (Cum. Supp. 1925) c. 126-15.

[52] N. Y. CONS. LAWS (Cahill, 1930) § 13 (3).

[53] OHIO GEN. CODE (Page, 1926) § 8321-1.

pend on the rightful application of the building loan installments. In that case both the owner and the lender would have a powerful motive to see that the money is used first for the lienor's benefit.

A large number of states have no legislation on the extent to which the rights of the legal title holder are affected by mechanics' liens arising from contracts made by lessees or vendees under executory contracts of sale. The few that do touch on the point vary greatly, and do not, in general, deal adequately with the question. But it seems clear that lienors may foreclose on the interests of such a vendee or lessee, and that the purchaser at the foreclosure sale gets all their rights on performing their covenants.[54] Several states provide that where the vendor or lessor has consented to the improvements, his interest is subject to the lien.[55] Where, however, there is no consent, and the lessee or vendee has forfeited his rights to the property the difficulty becomes apparent. Many statutes declare that the building may be sold to satisfy liens arising from building contracts made by the vendee or lessee,[56] but these statutes make no specific provision for the repair situation, with the exception of one which gives the claimant a lien on the building to the extent to which its value has been enhanced by his work.[57]

Section 3(2) of the Uniform Act provides that liens shall extend "to and only to the owner's [58] right, title or interest existing at the time of the visible commencement of operations, or thereafter acquired, in the real property." The effect of this provision is, by implication, to cut off liens for repairs on leased property. Such a result would be unhappy, in view of the purpose of a mechanics' lien act. It would seem preferable to give the claimant an express lien on the enhanced value of the property. Although such a provision would possibly work hardship on the owner, since he may find his property subjected to a foreclosure sale, yet he has probably benefited by the improvement, and in any event is in a superior position to the lienor in that he can usually prevent an alteration to his property unless the lease or contract of sale calls for it. In the latter situation, the Uniform Act, following a substantial authority among the state statutes

[54] KY. STAT. (Carroll, 1930) § 2463 is an example of this very general provision.

[55] See CAL. CODE OF CIV. PROC. (Deering, 1923) § 1192; as to what is consent, see Note (1930) 28 MICH. L. REV. 321, 326.

[56] Iowa Code (1931) § 10275; MONT. REV. CODES (1921) § 8343; *cf.* WYO. COMP. STAT. (1920) § 4865 (lienor may, in addition, by performing broken covenants, be subrogated to rights of lessee and enforce lien). For a similar provision where rights were those of vendee, see MICH. COMP. LAWS (1929) § 13103.

[57] KY. STAT. (Carroll, 1930) § 2464.

[58] By § 1 of the Uniform Mechanics' Lien Act the term "owner" includes a lessee or a vendee in possession under a contract for the purchase of real estate.

that such a contract shall be deemed a consent to be liable,[69] makes the owner's interest subject to the lien.

The Uniform Act makes no provisions as to foreclosure proceedings in liens. Since Sec. 37 repeals only acts or parts of acts "inconsistent" with the Uniform Act, the enforcement of liens is apparently to continue to follow the customary procedure of the several states.

THE LEGAL STATUS OF BOND PREMIUMS FOR INCOME TAX PURPOSES

THE controversy with regard to the legal status of bond premiums for income tax purposes was initiated in 1920 by the litigation involving the bonds of the Old Colony Railway Company. The bonds had been issued between the years 1895 and 1904[1] and sold at premiums aggregating $199,528.08 which were entered by the company in a special account entitled "Premium on Bonds." Subsequently, by order of the Interstate Commerce Commission, the premiums were amortized over the periods of the respective lives of bonds, and on the books of the company an aliquot part was then transferred each year to the profit and loss account. In 1920 the Commissioner of Internal Revenue sought to include in the taxable income of the company the amount of premiums apportioned for that year. The Board of Tax Appeals, however, concluded that the amortization of the bond premiums "cannot give rise to income where no transaction has occurred during the taxable year with reference to the sale, purchase, or payment of the bonds." [2] The Circuit Court of Appeals, for the First Circuit, though affirming the decision, based its affirmance on the constitutional ground that the premiums were received by the Old Colony prior to the effective date of the Income Tax Amendment.[3]

In order to reflect an aliquot part of the premiums in the Old Colony's net income for 1921, the Commissioner of Internal Revenue predicated his claim upon a new theory. Abandoning his former contention that the bond premiums constituted taxable

[1] In 1893 the Old Colony had leased its railroad lines to the New York, New Haven, and Hartford Railroad Company, under an arrangement whereby the New Haven was to operate the railroad and pay a certain rental, including all taxes. For an argument that the lease was a material factor in the subsequent decisions and that the case is, therefore, unsatisfactory for test purposes, see Brady, *Old Colony Railroad Case—Are Bond Premiums Income*, TAX MAGAZINE, September, 1931, at 317, 344.

[2] Old Colony Ry. Co. v. Commissioner, 6 B. T. A. 1025, 1027 (1927).

[3] Old Colony Ry. Co. v. Commissioner, 26 F. (2d) 408 (C. C. A. 1st, 1928). The Sixteenth Amendment to the Constitution was adopted February 23, 1913.

income, he argued that such premiums in reality represented the amount by which the nominal rate of interest on the bonds exceeded the effective rate, or the rate which the company would have paid had the bonds been sold on the market at par. Under this theory the interest actually paid each year on the bonds included an excess which was really not interest at all but merely the repayment of so much of the investment of the bond purchaser as was represented by the premium he had paid. Consequently, in computing income the Old Colony would not be entitled to deduct as a capital charge that part of the interest which represented an aliquot part of the premiums received.[4]

Whether the bond premiums are regarded as income or as "excess interest," the taxable net income of the company of course remains the same. The distinction, however, becomes of more than academic importance, where, as in the *Old Colony* case, the premiums have been received prior to the adoption of the Sixteenth Amendment giving Congress the power to levy or collect taxes on incomes without apportionment. Constitutional objections are not available if the premiums are to be regarded as "excess interest," since "what is income is controlled by the Constitution, while deductions are a statutory concept." [5] The Board of Tax Appeals, however, on the authority of the 1928 decision of the Circuit Court of Appeals, refused to accept the Commissioner's theory.[6] But the Circuit Court of Appeals, although speaking of the bond premiums as profit or income,[7] reversed the decision of the Board and allowed the Commissioner's claim,[8] relying largely on the converse case of *Western Maryland Ry. v. Commissioner*,[9] where bond discounts were held to be equivalent to additional interest payable upon maturity and

[4] The Commissioner's theory is outlined in the case of Fall River Electric Light Co. v. Commissioner, 23 B. T. A. 168, 170 (1931).

[5] Chicago, R. I. & Pacific Ry. v. Commissioner, 13 B. T. A. 988, 1029 (1928).

[6] Old Colony Ry. v. Commissioner, 18 B. T. A. 267 (1929).

[7] Bond premiums of course cannot constitute both income and "excess interest."

[8] Old Colony Ry. Co. v. Commissioner, 50 F. (2d) 896 (C. C. A. 1st, 1931). It seems apparent that the court was overruling its former decision in the 1920 case. Money which had previously been held non-taxable was held taxable, merely because the Commissioner's claim was predicated on a different theory. But the court endeavored to distinguish the 1920 case by saying, "The decision was that a profit made in 1904, before the passage of the Sixteenth Amendment to the Constitution of the United States, could not be taxed. The court's attention was not called to the fact that he profit made in the early years was not being taxed, but that it was being used only to determine the expense for the year 1921 of the payment of interest on the bonds. This is not a tax, but an allocation under proper accounting methods for books kept on the accrual basis, of the expense chargeable to the year 1921."

[9] 33 F. (2d) 695 (C. C. A. 4th, 1929).

therefore deductible proportionately each year of the life of the bond as interest accruing for that year.[10]

In the meanwhile, however, the Board of Tax Appeals, apparently without the knowledge of the court, overruled its former decision in the 1920 case and held in *Fall River Electric Light Co. v. Commissioner*[11] that bond premiums represent taxable income to be amortized over the life of the bonds. This most recent decision of the Board was largely based upon rules of statutory construction. Article 544 of Treasury Regulation 45, adopted under the Revenue Act of 1918, provides that ". . . if bonds are issued by a corporation at a premium, the net amount of such premium is gain or income which should be prorated or amortized over the life of the bonds."[12] The provisions of the Revenue Act of 1918 designed to regulate the determination of the taxpayer's net income have been reenacted without change in subsequent Acts.[13] Accordingly in the *Fall River* case the Board of Tax Appeals suggested that regulations which had so long been in force "should not be upset in the absence of a clear showing that they are contrary to the statute."[14] But regardless of the

[10] The similar decision of the Board in Chicago, R. I. & Pacific Ry. v. Commissioner, *supra* note 5, was also cited, apparently without the knowledge that it had been reversed in the interim by the Circuit Court of Appeals for the Seventh Circuit, 47 F. (2d) 990 (1931), in reliance on the court's own opinion in the 1920 Old Colony case.

[11] *Supra* note 4.

[12] 21 Treas. Dec. 289 (1919). Article 545 of Treasury Regulations 62, 65, and 69, and Article 68 of Treasury Regulation 74, enacted under the Revenue Acts of 1921, 1924, 1926, and 1928, respectively, contain the same provision. 24 Treas. Dec. 366 (1922); 26 Treas. Dec. 901 (1924); 28 Treas. Dec. 721 (1926).

[13] § 213 of the Revenue Act of 1918 provides "that . . . the term 'gross income' (a) includes gains, profit and income derived from . . . dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from . . . the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever." 40 STAT. 1065 (1918). § 234 (a) of the same Act provides "that in computing the net income of a corporation . . . there shall be allowed as deductions . . . (2) all interest paid or accrued within the taxable year on its indebtedness." 40 STAT. 1077 (1918). § 212 (b) provides that the "net income shall be computed upon the basis of the taxpayer's annual accounting period in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method has been employed, or if the method employed does not clearly reflect the income, the computation shall be made upon such basis and in such manner as in the opinion of the Commissioner does clearly reflect the income." 40 STAT. 1064 (1918). These provisions were all reenacted in the Revenue Acts of 1921, 1924, 1926, and 1928, and the cited Regulations of the Commissioner of Internal Revenue merely represent their "executive construction."

[14] Fall River Electric Light Co. v. Commissioner, *supra* note 4, at 174. See Brady, *op. cit. supra* note 1, at 320. It is apparent, however, that the Board was placing unprecedented emphasis upon the doctrine of "implied

importance of any rule of statutory construction, if bond premiums are not income within the meaning of the Sixteenth Amendment the Regulations must be disregarded.

Taxable income was defined by the Supreme Court in *Eisner v. Macomber* [15] as the "gain derived from capital, from labor, or from both combined, provided it be understood to include profit gained through a sale or conversion of capital." In *Bowers v. Kerbaugh Empire Co.*[16] that Court held that a plaintiff, who borrowed money from a bank in Germany before the War, repayable in marks or their equivalent in gold coin of the United States, and who repaid the loan when marks had greatly depreciated, did not realize profit or income to the extent of the depreciation, under the definition of income asserted in the *Eisner* case. But the same court has recently held in *United States v. Kirby Lumber Company* [17] that a corporation purchasing its own bonds at less than their issuing price realized income thereby. The *Kerbaugh* case was distinguished on the ground that the taxpayer in that case had lost the borrowed capital in the transaction for which he had borrowed it, whereas in the *Kirby* case the transaction resulted in "clear gain." But the profit or loss resulting from the use of borrowed capital does not seem to be material in determining whether any part of such capital constituted income when received.[18] The result of the *Kirby* case could have been achieved more consistently with the definition of income postulated in *Eisner v. Macomber* by adopting the Commissioner's "effective rate" theory, under which the repurchase of bonds at less than their issuing price indicates that the interest which the corporation had deducted as an expense each year during which the bonds were outstanding exceeded the legitimately deductible "effective rate" by an aliquot part of the discount at which the bonds were repurchased. The practical difficulty of disturbing old tax returns in order to include this excess

legislative sanction and approval." Indeed, the same tribunal, without mentioning this doctrine, had previously held in Independent Brewing Company v. Commissioner, 4 B. T. A. 870 (1926), that a corporation purchasing its own bonds for less than the amount at which they were issued realized no income thereby, despite the fact that Article 544 of Treasury Regulation 45 asserted a precisely contrary policy and was unaltered by the Revenue Act of 1921. This decision was followed in New Orleans, Texas, and Mexico Ry. v. Commissioner, 6 B. T. A. 436 (1927), and in Consolidated Gas Co. v. Commissioner, 24 B. T. A. — (Oct. 15, 1931). In the latter case the Board differentiated between the bonds themselves and interest coupons attached thereto, holding that the excess of the face value of the coupons over the amount paid for them was taxable as income.

[15] 252 U. S. 189, 207, 40 Sup. Ct. 189, 193 (1920).

[16] 271 U. S. 170, 46 Sup. Ct. 449 (1926).

[17] 52 Sup. Ct. 4 (U. S. 1931).

[18] See United States v. Kirby Lumber Co., 44 F. (2d) 885, 887 (Ct. Cl. 1931).

amount may have led the court to reason as it did,[19] but in the absence of this consideration, there would seem to be no reason why the Commissioner's theory should not be accepted. It seems apparent that bond premiums furnish a mere "increase in the capital reservoir," a "feeding by the springs of investment," and in this respect are similar to stock premiums,[20] which in the *Fall River* case the Board of Tax Appeals conceded could not be regarded as income.[21] Moreover, the classification of bond premiums as income seems inaccurate from an economic point of view, when it is considered that a corporation, barring bankruptcy, must inevitably pay back more than it receives from the sale of its bonds. Such a sale is purely a financing transaction in which the corporation contemplates profit from the use of the capital which is borrowed and not from the mere loan itself. The Supreme Court seems to have noted this distinction in *Eisner v. Macomber*, and, in pointing out the distinguishing attribute of income, said, "Here we have the essential matter: *not* a gain *accruing* to capital, *not* a *growth* or *increment* of value *in* the investment; but a gain, a profit, something of exchangeable value *proceeding from* the property, *severed from* the capital however invested or employed." [22]

If it be conceded that bond premiums are not "income" within the meaning of the Sixteenth Amendment, it would seem that the Commissioner's excess interest theory should be adopted, for otherwise a corporation, by selling bonds with a high nominal interest rate, could reduce its net income by the amount of the premium received, and thus escape taxation *pro tanto*. This consideration may have induced the Board of Tax Appeals in the *Fall River* case to classify bond premiums as income when it felt itself constrained to reject the Commissioner's "excess interest" theory. While appreciating the possible significance of "effective interest" or "excess interest" in accounting practice, with respect to bond premiums, the Board was not willing to assume "that Congress . . . in granting to a taxpayer the right, in computing net taxable income, of deducting . . . 'all interest paid or accrued . . . on its indebtedness,' [23] had in mind such a theory and used this term in the restricted sense denoted in accounting parlance as 'effective interest' to the exclusion of a portion of the interest paid." [24] The Board further suggested

[19] See Comment (1931) 40 YALE L. J. 960.

[20] For an excellent argument to this effect see the dissenting opinion of Murdock, J., in the Fall River case, *supra* note 4, at 175.

[21] *Supra* note 4, at 173.

[22] *Supra* note 15, at 207, 40 Sup. Ct. at 193.

[23] Revenue Act of 1926 § 234 (a) (2).

[24] Fall River Electric Light Co. v. Commissioner, *supra* note 4, at 171. *Cf.* the opinion of the same tribunal in Chicago, R. I., and Pacific Ry. v. Commissioner, *supra* note 5, allowing the deduction of an aliquot part of

that "interest on indebtedness has a definite and well accepted meaning as the 'compensation allowed by law or fixed by the parties for use, or forbearance, or detention of money'," and, "we think it clear that the word 'interest' as used in the cited provision of the taxing act is to be understood in its ordinary sense." [25] By basing its conclusion solely on a question of the legislative intent to include the Commissioner's theory the Board precluded any inquiry into its validity. Yet accounting authorities agree that the sale of bonds at a premium merely indicates that the interest rate is higher than it need be were the bonds marketable at par.[26] This view seems to have been recognized by the Board of Tax Appeals itself in *Chicago, R. I., & Pacific Ry. v. Commissioner*,[27] where it conceded that it is immaterial whether bonds sold at par carry the market rate of interest, or whether if sold at a premium they carry a higher rate, or a lesser one if sold at a discount, since, other things being equal, the rate of interest finally paid will be the market and not the contract rate. Where a corporation provides that its bonds shall carry a high nominal interest rate, in order to sell them at a premium, the transaction seems in effect an offer to sell the bonds to the purchaser who is willing to take the greatest reduction of interest, the amount of the reduction to be paid by him in advance in the form of a premium.[28] Even though Congress may not have directly contemplated the Commissioner's "excess interest" theory, it seems reasonable to assume that in using the term "interest" Congress did have in mind interest as paid in the typical loan transaction, where no discount or premium is involved. Such interest represents the "effective rate" for which the Commissioner contends. Moreover, whether or not the term "interest" as understood in its "ordinary sense" excludes the Commissioner's theory is at least debatable. The courts seem to agree that a corporation may deduct as an expense for the taxable year an aliquot part of any discount at which its bonds were sold in addition to the interest paid its bondholders.[29] And

bond discounts. In order to reconcile the two opinions it is necessary to assume that Congress contemplated the Commissioner's theory of "effective interest" with respect to bond discounts but not with respect to bond premiums. Such an assumption appears absurd.

[25] Fall River Electric Light Co. v. Commissioner, *supra* note 4, at 171.

[26] HATFIELD, ACCOUNTING (1929) 90, 227, 228; 2 KESTER, ACCOUNTING THEORY AND PRACTICE (1925) 370, 393; SALIERS, ACCOUNTS IN THEORY AND PRACTICE (1920) 169, 171; DICKINSON, ACOUNTING PRACTICE AND PROCEDURE (1917) 66, 134, 135.

[27] *Supra* note 5, at 1031.

[28] See the dissenting opinion of Seawell, J., in the Fall River case, *supra* note 4, at 176.

[29] Western Maryland Ry. Co. v. Commissioner, *supra* note 9; Chicago, R. I. & Pacific Ry. v. Commissioner, *supra* note 5.

if it be admitted that bond discounts in an original sale are "deferred interest" the argument by analogy that bond premiums are "excess interest" seems to be logically irrefutable.

LIMITATIONS ON THE RIGHT OF THE LESSOR UNDER AN OIL AND GAS LEASE TO PROTECTION AGAINST DRAINAGE

FROM a relatively early date the courts recognized that in the absence of express stipulations the lessee of an ordinary oil and gas lease, after oil had been found in paying quantities, was under an implied obligation reasonably to develop the premises.[1] Such a duty was held to comprise the duty of drilling additional wells [2] and the duty of protecting the leased property from drainage through wells on adjacent land,[3] which not infrequently were owned by the lessee himself. In an effort to avoid the incubus of these duties, mining corporations soon devised the "or" lease, in which the lessee covenants to drill a stipulated number of wells or pay "delay rentals," [4] and the "unless" lease, which imposes no "duty" of development but automatically terminates unless the lessee drills a specified number of wells within a designated period or pays rentals for the privilege of deferring operations.[5] But even under these leases, the lessee, although in a measure relieved of his obligation to drill additional wells,[6] must still protect the leased premises from drainage.[7]

[1] Harris v. Ohio Oil Co., 57 Ohio 118, 123, 48 N. E. 502, 505 (1897); see Stoddard v. Emery, 128 Pa. 436, 442, 18 Atl. 339 (1889); *cf.* New State Oil & Gas Co. v. Dunn, 75 Okla. 141, 142, 182 Pac. 514 (1919); W. T. Waggoner Estate v. Sigler Oil Co., 118 Tex. 509, 517-519, 19 S. W. (2d.) 27, 29 (1929).

[2] Kleppner v. Lemon, 176 Pa. 502, 35 Atl. 109 (1896); *cf.* Ryan v. Kent, 36 S. W. (2d) 1007, 1011 (Tex. Comm. App. 1931). But *cf.* Venture Oil Co. v. Fretts, 152 Pa. 451, 25 Atl. 732 (1893).

[3] Blair v. Clear Creek Oil & Gas Co., 148 Ark. 301, 230 S. W. 286 (1921); Notes (1922) 19 A. L. R. 437 (1929) 60 A. L. R. 950; *cf.* Jones v. Interstate Oil Corporation, 1 Pac. (2d) 1051 (Cal. App. 1931). A Kentucky statute now makes compulsory the drilling of off-sets. KY. STAT. (Carroll, 1930) § 3766b-4c; *cf.* TEX. COMP. STAT. (1928) §§ 5369, 5370 (asylum and school lands). The Legislature may also limit the right to offset. Oxford Oil Co. v. Atlantic Oil Producing Co., 22 F. (2d) 597 (C. C. A. 5th, 1927). As to the constitutionality of statutes limiting production, see authorities cited *infra* note 35.

[4] See SUMMERS, LAW OF OIL AND GAS (1927) § 215.

[5] See form lease "Midcontinent 88."

[6] Southwestern Oil Co. v. McDaniel, 71 Okla. 142, 175 Pac. 920 (1918). But *cf.* Ohio Valley Oil & Gas Co. v. Irvin Development Co., 184 Ky. 517, 212 S. W. 110 (1919) (lessee cannot by paying "nominal" rentals postpone development indefinitely).

[7] Texas Co. v. Ramsower, 7 S. W. (2d) 872 (Tex. Comm. App. 1928). In West Virginia, the lessee under an "or" lease is not liable for damages during the period in which he has paid delay rentals, but if he has failed

The basis for the implication of these duties of development and protection was found in the nature of oil leases and in public policy considerations. The sole remuneration received by the lessor in the earlier leases was in the nature of royalties received from the actual production and marketing of the oil pumped,[8] and, argued the courts, if the lessee were left to his own devices, he would hold the lease for speculation, thereby depriving the lessor of his rent.[9] Furthermore, because of the peculiar mobile nature formerly attributed to oil and gas,[10] it was supposed that the lessor, himself unable to go on the land and drill during the term,[11] might be completely deprived of his minerals by delinquency on the part of the lessor in drilling. Finally, in the early days of oil production, the courts believed it in the public interest to have oil lands developed as rapidly and exhaustively as possible.[12] These considerations, which led to a policy rule of construction against the lessee and in favor of the lessor,[13] are responsible for the implementing of the duties to develop and pro-

to drill protection wells during that time he may have his lease forfeited at the end of the rental period, the obligation to protect being construed as a condition subsequent rather than a covenant. Carper v. United Fuel Gas Co., 78 W. Va. 433, 89 S. E. 12 (1916). But *cf.* Chapman v. Kendall, 145 Okla. 107, 291 Pac. 97 (1929) ("substantial" rentals), and cases of waiver, note 19 *infra.*

On similar grounds it would seem that the lessee under an "unless" lease, although under no duty either to drill or to pay, must nevertheless protect the leased premises from drainage. See Note (1930) 67 A. L. R. 221-236.

[8] See Acme Oil & Mining Co. v. Williams, 140 Cal. 681, 684, 74 Pac. 296, 297 (1903); *cf.* Ezzell v. Oil Associates, 180 Ark. 802, 807-808, 22 S. W. (2d) 1015, 1017 (1930).

[9] See Steelsmith v. Gartlan, 45 W. Va. 27, 35, 29 S. E. 978, 981 (1898); Huggins v. Daley, 99 Fed. 606, 613 (C. C. A. 4th 1899); *cf.* Monarch Oil, Gas & Coal Co. v. Richardson, 124 Ky. 602, 607, 99 S. W. 668, 669 (1907); Twin Lick Oil Co. v. Marbury, 91 U. S. 587, 592-593 (1875).

[10] See State v. Ohio Oil Co., 150 Ind. 21, 30, 49 N. E. 809, 812 (compared to ferae naturae); *cf.* Standard Oil Co. of Louisiana v. Giller, 38 S. W. (2d) 766 (Ark. 1931). But *cf.* Sigler Oil Co. v. W. T. Waggoner's Estate, 276 S. W. 936, 940 (Tex. Civ. App. 1925) (wild-cat territory) *aff'd* in 118 Tex. 509, 19 S. W. (2d) 27 (1929). For a discussion of the "ancient" conceptions of the mobility of oil and gas, see Veasy, *Law of Oil and Gas* (1920) 18 MICH. L. REV. 445, 452.

[11] Funk v. Haldeman, 53 Pa. 229, 248 (1866); *cf.* O'Neil v. Sun Co., 58 Tex. Civ. App. 167, 123 S. W. 172 (1909) (lessor required to account for lessee's share of oil produced from offset drilled by lessor). The lessee is usually given "an exclusive right" under the lease.

[12] See Parish Fork Oil Co. v. Bridgewater Gas Co., 51 W. Va. 583, 42 S. E. 655, 660 (1902); Brown v. Vandergrift, 80 Pa. 142, 148 (1875); *cf.* Crain v. Pure Oil Co., 25 F. (2d) 824, 831 (C. C. A. 8th 1928).

[13] See Emery v. League, 31 Tex. Civ. App. 474, 480, 72 S. W. 603, 607 (1903); Kies v. Williams, 190 Ky. 596, 600, 228 S. W. 40, 42 (1921); *cf.* Bettman v. Harness, 42 W. Va. 433, 447-448, 26 S. E. 271, 276 (inequality of bargaining power between lessor and lessee a consideration); Bortz v. Norris, 248 Mich. 247, 251-2, 226 N. W. 860, 861 (1929).

tect into the lease as implied covenants or conditions subsequent,[14] a breach of which may effect a termination of the lease,[15] be evidence of an intent to abandon,[16] or serve as the basis for a suit by the lessor to recover damages,[17] or have the lease forfeited.[18]

It was never supposed, however, that the lessor acquired an

[14] The obligation to protect is usually considered a covenant rather than a condition. SUMMERS, *op. cit. supra* note 4, at 453 and authorities there cited, n. 20. With the recognition of the lessor's power to claim a forfeiture for breach of this obligation, it became a condition as well. *Ibid.* 457-460. In Texas, where the lessee's interest is construed as a determinable fee in the minerals, the obligation has been alternately held a special limitation and a condition subsequent. See Walker, *The Nature of Property Interests Created By An Oil And Gas Lease in Texas* (1930) 8 TEX. L. REV. 483, 501. Development is not a duty but a condition in an "unless" lease. See Note (1930) 67 A. L. R. 223, 224. For a discussion of the nature of the legal interests ordinarily created by a lease, see SUMMERS, *op. cit. supra* note 4, c. 8.

[15] Stephenson v. Calliham, 289 S. W. 158 (Tex. Civ. App. 1926); Hall v. Augur, 82 Cal. App. 594, 256 Pac. 232 (1927); *cf.* Tedrow v. Shaffer, 23 Ohio App. 343, 155 N. E. 510 (1926); United States v. Brown, 15 F. (2d) 565, 567 (N. D. Okla. 1926). As to termination under the modern lease, see Marshall and Meyers, *Legal Planning of Petroleum Production* (1931) 41 YALE L. J. 33, 45, n. 42. The lessor must exercise his option of forfeiture under an "or" lease. Allen v. Narver, 178 Cal. 202, 172 Pac. 980 (1918). No such affirmative action is necessary under an "unless" lease, time being furthermore "of the essence." Abell v. Bishop, 86 Mont. 478, 284 Pac. 525 (1930).

[16] Mitchell, Jones & May v. Dabney, 294 S. W. 243 (Tex. Civ. App. 1927); *cf.* Fox Petroleum Co. v. Booker, 123 Okla. 276, 253 Pac. 33 (1926) (no "relinquishment" necessary in oil and gas lease, lessee having no title). See criticism of the doctrine of abandonment in Texas, Walker, *op. cit. supra* note 14, 7 TEX. L. REV. 589-596, 8 *ibid.* 505-511. Compare Leonard v. Prater, 36 S. W. (2d) 216, 221 (Tex. Comm. App. 1931), with the same case in 18 S. W. (2d) 681 (Tex. Civ. App. 1929).

[17] Kellar v. Craig, 126 Fed. 630 (C. C. A. 4th 1903); see Note (1922) 19 A. L. R. 450; *cf.* Note (1930) 39 YALE L. J. 431. The court may also decree that further development be made. Webb v. Croft, 120 Kan. 654, 244 Pac. 1033 (1926). Such a decree, however, will not be granted under an "unless" lease. See MERRILL, COVENANTS IMPLIED IN OIL AND GAS LEASES (1926) 246; Fox Petroleum Co. v. Booker, *supra* note 16, at 279, 280, 253 Pac. at 35, 36.

[18] An exception to the "rule" that "equity abhors a forfeiture" is made in the case of oil and gas leases. Robinson v. Miracle, 146 Okla. 31, 32, 293 Pac. 211, 212 (1930). The Kentucky court no longer recognizes this exception. Conley v. Wheeler-Watkins Oil & Gas Co., 216 Ky. 494, 500, 288 S. W. 350, 352 (1926); Johnson v. Dodson, 227 Ky. 132, 137, 12 S. W. (2d) 310, 312 (1928). But *cf.* Monarch Oil, Gas, & Coal Co. v. Richardson, *supra* note 9. The Kentucky Legislature, however, has recently passed a statute requiring forfeiture for failure to protect. KY. STAT. (Carroll, 1930) § 3766b-4c. *Cf.* MONT. REV. CODES (Choate, 1921) § 6902 (provision for release from record after forfeiture). The attitude of the Texas Court of Civil Appeals is anomalous and inconsistent. *Cf.* Stephenson v. Calliham, *supra* note 15 (forfeiture decreed); Hanover Co. v. Hines, 11 S. W. (2d) 621 (1928) (failure to develop "requires exercise of court's equity powers"); Leonard v. Prater, *supra* note 16, at 221.

unqualified right to protection under these implied covenants. By injudiciously accepting a delay rental he might waive it.[19] In some states he is required to give a prescribed form of notice allowing the lessee a reasonable time to act thereon.[20] A stipulation in the lease as to the number of additional wells that are to be drilled may also be held a limitation of the lessee's duty to drill offsets.[21] Finally, his right may be defeated if the defendant can prove that in not drilling an offset he had acted as an ordinarily prudent operator, having regard to the interests of both parties.[22] Under this general defense, the lessee may show that the adjacent wells which the lessor wished offset were not producers,[23] that there was no imminent or substantial danger of drainage,[24] or possibly that an offset would not prove profitable,[25] the lessor bearing the burden of proof on all these issues,[26] and "due deference" being given to the lessee's judgment.[27] A few jurisdictions have even held the lessee's *bone fide* judgment binding on the

[19] Clear Creek Oil & Gas Co. v. Brunk, 160 Ark. 574, 255 S. W. 7 (1923); Orr v. Comar Oil Co., 46 F. (2d) 59 (C. C. A. 10th 1930); *cf.* Texas Co. v. Ramsower, *supra* note 7, at 876 (lessor must "intend" acceptance of the rental as a waiver).

[20] Johnson v. Dodson, *supra* note 18; Wapa Oil & Development Co. v. McBride, 84 Okla. 184, 201 Pac. 984 (1921). But *cf.* Solberg v. Sunburst Oil & Gas Co., 76 Mont. 254, 246 Pac. 168 (1926); Calhoma Oil Corporation v. Conniff, 207 Cal. 648, 279 Pac. 771 (1929); Harris v. Kerns, 144 Okla. 225, 291 Pac. 100 (1930) (bringing of suit sufficient notice of intent to forfeit under "or" lease). In the principal case of Leeper Oil Co. v. Rowland, *infra* note 37, the court held the notice insufficient.

[21] O'Neil v. Sun Co., *supra* note 11; *cf.* Stoddard v. Emery, *supra* note 1; But *cf.* Brewster v. Lanyon Zinc Co., 140 Fed. 801, 810-811 (C. C. A. 8th, 1905); Culbertson v. Iola Portland Cement Co., 87 Kan. 529, 125 Pac. 81 (1912); MERRILL, *op. cit. supra* note 17, § 64. The lessor's right to protection may also be limited by agreement. Linn v. Wehrle, 35 Ohio App. 107, 172 N. E. 288 (1928). *Cf.* Davis v. Mose, 112 Okla. 38, 239 Pac. 447 (1925) (payment in lieu of drilling). But *cf.* Jones v. Interstate Oil Corporation, *supra* note 3. Or by statute. Oxford Oil Co. v. Atlantic Oil Producing Co., *supra* note 3; R. R. Commission of Texas v. Bass, 10 S. W. (2d) 586 (Tex. Civ. App. 1928).

[22] Brewster v. Lanyon Zinc Co., *supra* note 21, at 814; Hays v. Bowser, 158 S. E. 169 (W. Va. 1931); *Cf.* Ohio Oil Co. v. Reichert, 343 Ill. 560, 567, 175 N. E. 790, 793 (Ill. 1931).

[23] Franklin v. Wigton, 132 Okla. 236, 270 Pac. 1 (1928); *cf.* Pelham Petroleum Co. v. North, 78 Okla. 39, 188 Pac. 1069 (1920); Humble Oil & Refining Co. v. Poe, 29 S. W. (2d) 1019 (Tex. Comm. App. 1930).

[24] Doiron v. Calcasieu Oil Co., 172 La. 553, 134 So. 742 (1931). Compare Goodwin v. Standard Oil Co., 290 Fed. 92, 98 (C. C. A. 8th, 1923) with Ohio Fuel Supply Co. v. Shilling, 101 Ohio 106, 109, 123 N. E. 873, 874 (1920).

[25] State Line Oil & Gas Co. v. Thomas, 35 S. W. (2d) 746 (Tex. Civ. App. 1931); *cf.* Ward v. Daugherty, 228 Ky. 326, 14 S. W. (2d) 1089 (1929).

[26] Texas Pacific Coal & Iron Co. v. Barker, 117 Tex. 418, 6 S. W. (2d) 1031 (1928) (amount and value of oil or gas product must be alleged and proved), and cases cited *supra* notes 23-25.

[27] *Cf.* Union Gas & Oil Co. v. Diles, 200 Ky. 188, 254 S. W. 205 (1923); Weisant v. Follett, 17 Ohio App. 371 (1922).

court.[28]

Those jurisdictions that have defined the lessee's duty in terms of "the ordinarily prudent operator" have weighed the amounts already expended by the lessee in exploring, drilling, transporting, and marketing in relation to his net profits against the royalties already received by the lessor,[29] placing increasing emphasis on the fact that the lessor has everything to gain and nothing to lose from the drilling of new wells, whereas the lessee must undergo large expense and great risks with perhaps insufficient returns therefore.[30] Likewise considered have been the quality and character of the oil and gas stratum,[31] the proximity of a profitable market and the costs of transportation thereto.[32] There has also appeared a tacit recognition that the reasons for the

[28] This is the Pennsylvania doctrine. Colgan v. Forest Oil Co., 194 Pa. 234, 45 Atl. 119 (1899); But see Highfield Co. v. Kirk, 248 Pa. 19, 22-23, 93 Atl. 815, 817 (1915). West Virginia seems to confuse the two standards. Jennings v. Southern Carbon Co., 73 W. Va. 215, 80 S. E. 368 (1918) (failure to exercise ordinary prudence constitutes "fraud"); Blue Creek Development Co. v. Howell, 101 W. Va. 748, 133 S. E. 699 (1926) (unjust enrichment). The Kentucky court has recently adopted the majority rule. Swiss Oil Corporation v. Risner, 223 Ky. 397, 3 S. W. (2d) 777 (1928).

The "good faith" standard has been criticized in Brewster v. Lanyon Zinc Co., *supra* note 21, at 812-815, and in Texas Co. v. Ramsower, *supra* note 7, at 874-875. But *cf.* Little v. Stephenson, 1 S. W. (2d) 353 (Tex. Civ. App. 1927). That its too strict application may lead to evident injustice, see the case of Barnard v. Monongahela Natural Gas Co., 216 Pa. 362, 65 Atl. 801 (1907) (lessor refused protection against drainage though robber wells operated by lessee because lessee's action not "a fraud per se").

[29] Hart v. Standard Oil Co., 146 La. 885, 84 So. 169 (1920) (lessee's expenditures, $650,000 with little profit; lessor's royalties, $90,000); Austin v. Ohio Fuel Oil Co., 218 Ky. 310, 291 S. W. 386 (1927) (total expenditures over $37,000; total realized $41,000 without deduction for depreciation, taxes, and overhead). *Cf.* Johnson v. Dodson, *supra* note 18 (19,000 expended and record "fails to show even approximately" income received therefrom). See also Union Gas & Oil Co. v. Fyffe, 219 Ky. 640, 294 S. W. 176 (1927).

[30] See Swiss Oil Corporation v. Risner, *supra* note 28, at 401, 3 S. W. (2d) at 778 (the lessor "does nothing but cogitate over his contemplated royalties and collects and enjoys them after they come"); *cf.* Goodwin v. Standard Oil Co., *supra* note 24, at 95.

[31] Indiana Oil and Gas Development Co. v. McCrory, 42 Okla. 136, 145, 140 Pac. 610, 614 (1914); *cf.* McKnight v. Manufacturer's Natural Gas Co., 146 Pa. 185, 23 Atl. 164 (1892); Allen v. Colonial Oil Co., 92 W. Va. 689, 115 S. E. 842 (1923). Compare Bryan v. Sinclair Oil & Gas Co., 1 S. W. (2d) 917 (Tex. Civ. App. 1927), with Sinclair Oil & Gas Co. v. Bryan, 291 S. W. 692, 695 (Tex. Civ. App. 1927). See also Becker v. Submarine Oil Co., 55 Cal. App. 688, 204 Pac. 245 (1921) (extent of oil reservoir).

[32] Strange v. Hicks, 78 Okla. 1, 188 Pac. 347 (1920). Compare Pennagrade Oil & Gas Co. v. Martin, 211 Ky. 137, 277 S. W. 302 (1926), with Pryor Mountain Oil & Gas Co. v. Cross, 31 Wyo. 9, 222 Pac. 570 (1924). See also Hanks v. Magnolia Petroleum Co., 24 S. W. (2d) 5 (Tex. Crim. App. 1930).

The rule requiring development seems somewhat relaxed in "wildcat" territory. Houston v. Highland Oil Co., 6 La. App. 325 (1926).

earlier policy of protection to the lessor are failing.[33] The lessor now is often given a substantial consideration, either as an inducement for the lease or by way of valuable rentals, and is thus no longer exclusively dependent upon his royalties for remuneration.[34] And some courts seem at last aware that the public is today interested in conservation rather than intensive development of oil fields.[35] Finally, the presence of a demoralized oil market making it to the advantage of the lessor as well as the lessee to sacrifice present development has received implicit recognition in a few recent decisions.[36]

The recent case of *Leeper Oil Co. v. Rowland*[37] seems indicative of the new trend in the construction of oil and gas leases. In this case, under a lease executed in 1919, four producing wells had

[33] See O'Donnell v. Snowden & McSweeney Co., 237 Ill. App. 156, 165 (1925), *aff'd* in 138 Ill. 374, 149 N. E. 253 (1926); Bouldin v. Gulf Production Co., 5 S. W. (2d) 1019, 1023 (Tex. Civ. App. 1928).

[34] *Cf.* Smith v. Louisiana Refining Corporation, 12 F. (2d) 378 (C. C. A. 8th 1926) ($12,500 initial consideration); Leonard v. Prater, *supra* note 16 (contingent bonus of $5,000). For a valuable and exhaustive discussion of what consideration will support a lease; see Union Gas & Oil Co. v. Wiedeman Oil Co., 211 Ky. 361, 277 S. W. 323 (1924). *Cf.* SUMMERS, *op. cit. supra* note 4, at 381. But *cf.* Jones v. Interstate Oil Corporation, *supra* note 3, at 1053.

[35] *Cf.* Oxford Oil Co. v. Atlantic Oil Producing Co., *supra* note 3; Julian Oil & Royalties Co. v. Capshaw, 145 Atl. 237, 292 Pac. 841 (1930); People v. Associated Oil Co., 211 Cal. 93, 96-97, 294 Pac. 717, 723 (1930); People v. Associated Oil Co., 297 Pac. 536 (Cal. 1931). See Nevada Consolidated Copper Co. v. Consolidated Coppermines Corporation, 44 F. (2d) 192, 198 (D. C. Nev. 1930). For legislative conservation of oil resources, see Legislation (1931) 31 COL. L. REV. 1170, 1172 ff.; Note (1930) 43 HARV. L. REV. 1137; Note (1930) 67 A. L. R. 1347.

[36] *Cf.* Transcontinental Oil Co. v. Thomas, 29 F. (2d) 733 (C. C. A. 5th 1928) (lack of market a defense for failure to develop); Austin v. Ohio Fuel Co., *surpa* note 29, at 312-313, 291 S. W. at 387; Beech Fork Coal Co. v. Pocahontas Corporation, 109 W. Va. 39, 152 S. E. 785 (1930); Steven v. Potlatch Oil and Refining Co., 80 Mont. 239, 260 Pac. 119 (1929); Smith v. Sun Oil Co., 135 So. 15 (La. 1931) (since no available market, no production in "paying quantities"). See also cases *supra* note 32. But *cf.* Carroll Gas & Oil Co. v. Skaggs, 231 Ky. 278, 21 S. W. (2d) 445 (1929) (failure to market gas ground for suit). A few *dicta* in other periods of oil "overproduction" have apparently been ignored. See for example Paraffine Oil Co. v. Cruce, 63 Okla. 95, 100-103, 162 Pac. 716, 721-723; Note (1917) 14 A. L. R. 967; Brewster v. Lanyon Zinc Co., *supra* note 21, at 813-814. But see Masterson v. Amanillo Oil Co., 253 S. W. 908, 912 (Tex. Civ. App. 1923) ("financial depression throughout the country no excuse" for non-development). A distinction has been made between the failure to market oil and the failure to market gas, the latter obligation not being so strictly enforced, since the lessor's royalties are usually not dependent, as in the case of oil, on the actual sale of the product but rather on the number of gas wells drilled. *Cf.* Howerton v. Kansas Natural Gas Co., 82 Kan. 367, 108 Pac. 813 (1910); see Union Gas & Oil Co. v. Fyffe, *supra* note 29, at 643-644, 294 S. W. at 177-178.

[37] 39 S. W. (2d) 486 (Ky. 1931).

been drilled and exploited to their full capacity and were yielding at the date of suit one and a third barrels per day. Since 1923, however, no additional wells had been drilled despite conceded drainage by wells of equivalent capacity operated on adjacent territory and also owned by the lessee. The plaintiff, after repeatedly requesting the lessee to offset these wells, brought suit to compel development of his tract of land, or in the alternative, for cancellation of the lease. There was no provision in the lease for delay rentals or for forfeiture. The lessees relied "as their chief defense" on their contention that "the lease had been already drilled and developed as much as conditions of the market and cost of operation justified, and that under the existing and prevailing conditions in the oil business it would be imprudent and with sacrifice and loss to the parties concerned to develop further at the present time." Ignoring this defense, the trial court decreed that the lessee should forthwith drill another well and should it prove a producer the lessee should sink three wells a year, or, in its discretion, cancel the lease. The Kentucky Court of Appeals, although acknowledging the defendant's implied duty diligently and in good faith to develop the premises, took cognizance of the defense and held that the lessee, as a reasonably prudent operator, was under no duty to make further development at the time. To achieve this result the court took judicial notice of "the nation-wide depression" particularly in its effect upon the oil industry, emphasizing the overproduction and consequent "ruinously low" prices of oil, and in effect suggesting that unfavorable market conditions may in themselves defeat the lessor's right to protection.[38]

Commendable as this result may at first seem as a step towards the readjustment of oil and gas law to modern conditions, it may give rise to certain very tangible evils. If the lessee's duty to offset is to be defined in terms of a highly-fluctuating market, leases will be rendered nugatory, the lack of certainty as to rights and duties under them will be increased, and courts will find themselves functioning in the capacity of supervisory industrial commissions. That the price of oil has an important bearing on the profitability of development and protection and consequently on the standards to be expected of a reasonably prudent operator cannot be denied. But to hold that the current price of oil, which cannot be gauged as high or low without reference to the entire price structure, is determinative of the extent of the lessee's duty seems a dangerous precedent.

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[38] Oil was selling at about $1.50 a barrel when suit was brought and had declined considerably since "the time of trial of this action." The Kentucky statute, *supra* note 3, was enacted after the execution of the lease and was held to have no retroactive effect. See also note 20, *supra*.

More easily might the Kentucky court have rested its decision upon the failure of the lessor to show by a preponderance of the evidence that the lessee could have drilled a profitable offset.[39] Since the lessee was also operating the robber wells, however, it would seem that, regardless of the question of profit, the lessor should in good conscience receive royalties for as much of the oil produced on adjacent territory as he could show was being drained from his premises.[40] The obstacles in the way of such a showing are but some of the difficulties presented by this case, which might well serve to illustrate the thesis that relief of the oil industry must be sought not in sporadic judicial measures but in governmental supervision and control of unit operation.[41]

THE ADMINISTRATION OF BAIL

AFTER the most thorough examination of a bail system which has been undertaken in any jurisdiction an investigator has concluded that its breakdown is in large measure attributable to the failure of courts to avail themselves of the potential flexibility of the bail law.[1] This conclusion was advanced in face of the fact that in the jurisdiction in which the survey was conducted, as in most others, comprehensive constitutional and statutory provisions attempt to regulate the bail system in detail. Thirty-five states by constitution [2] and one by statute [3] guarantee that, "All persons shall be bailable by sufficient sureties except for capital offenses where the proof is evident or the presumption great." Four except only murder and treason from

[39] As in the cases cited in note 25, *supra*.

[40] *Cf.* Note (1922) 19 A. L. R. 437, 443. This was the course adopted in Culbertson v. Iola Portland Cement Co., *supra* note 21. Compare the deplorable result reached in Barnard v. Monongahela Natural Gas Co., *supra* note 28.

[41] *Cf.* Marshall and Meyers, *op. cit supra* note 15, at 48, 63-64 *et passim*. In Union Oil & Gas Co. v. Fyffe, *supra* note 29, the court actually attempted a "judicial" form of unit operation of a block of gas fields.

[1] BEELEY, BAIL SYSTEM IN CHICAGO (1927) 160.

[2] ALA., art. I, § 16; ARIZ., art. II, § 22; ARK., art. II, § 8; CAL., art. I, § 6; COLO., art. II, § 19; CONN., art. I, § 14; DEL., art. I, § 12; FLA., Declaration of Rights, § 9; IDAHO, art., I, § 6; ILL., art. II, § 7; IOWA, art. I, § 12; KAN., Bill of Rights, § 9; KY., Bill of Rights, § 16; LA., art. 12; ME., art. I, § 10; MINN., art. I, § 7; MISS. art. III, § 29; MO., art. II, § 24; MONT., art. III, § 19; N. D., art. I, § 6; NEV., art. I, § 7; N. J., art. I, § 10; N. M., art. II, § 13; OHIO, art. I, § 9; OKLA., art. II. § 8; PA., art. I, § 14; S. C., art. I, § 20; S. D., art. VI, § 8; TENN., art. I, § 15; TEX., art. I, § 2; UTAH, art. I, § 8; VT., § 32; WASH., art. I, § 20; WIS., art. I, § 8; WYO., art. I, § 14. Unless otherwise stated the article and section refer to the state constitution.

[3] New Hampshire, PUBLIC STATUTES, 1926, c. 366, § 13.

the constitutional guarantee.[4] In many situations this absolute guarantee of bail in most offenses has brought about undesirable results which would probably have been avoided in those states [5] which enforce the common law rule allowing magistrates practically unlimited discretionary power to grant or refuse bail.[6] If bail is a matter of right, the magistrate may not refuse it, even though the petitioner has previously absconded and it is probable that he will again abscond,[7] and even though he is accused of an offense committed while on bail previously granted.[8] The remedy for these conditions lies in the difficult field of constitutional revision.[9]

However, even in those jurisdictions which guarantee bail in the terms quoted above, the effect of judicial action is fundamental. Thus, in interpreting and applying the clause excepting from the guaranty capital cases where the proof is evident or the presumption great, courts have arrived at strikingly different results. In Oklahoma and two other states the burden is placed on the applicant to show that the proof is not evident nor the presumption great;[10] in Texas and three other states the burden is on the prosecution.[11] Moreover, in determining what weight shall be given an indictment for a capital offense, jurisdictions have arrived at widely different results. In three states the indictment is conclusive that proof of guilt is evident;[12] in seven it creates

[4] IND. CONST., art. I, § 17; MICH. CONST., art. II, § 14; NEB. CONST., art. I, § 9; ORE. CONST., art. I, § 14.

[5] Massachusetts, New Hampshire, North Carolina, Virginia, and West Virginia. In three states statutes provide that bail is a matter of right where the offense charged is a misdemeanor. GA. PEN. CODE (1926) § 958; MD. ANN. CODE (Bagby 1924) art. 52, § 12; N. Y. CODE CRIM. PROC. (Gilbert 1920) § 553.

[6] Rex v. Baltimore, 4 Burr. 2180 (1768); Rex v. Rudd, 1 Cowp. 331 (1775). This is apparently still the law in England. 9 HALSBURY, LAWS OF ENGLAND (1909) 323.

[7] Rowan v. Randolph, 268 Fed. 527 (C. C. A. 7th, 1920); Kendrick v. State, 180 Ark. 1160, 24 S. W. (2d) 859 (1930). But if bail is discretionary, it will be refused. In re Lamar, 294 Fed. 688 (D. N. J. 1924).

[8] See SUTHERLAND, CRIMINOLOGY (1924) 213, where reference is made to a case in which a criminal released on bail was re-arrested four times for fresh crimes and each time admitted to bail.

[9] See I CODE OF CRIMINAL PROCEDURE (Am. L. Inst. 1928) § 10.

[10] *Ex parte* Decker, 37 Okl. Cr. Rep. 105, 257 Pac. 332 (1927); *Ex parte* Andrews, 39 Okl. Cr. Rep. 359, 265 Pac. 144 (1928); *Ex parte* Paige, 82 Cal. App. 576, 255 Pac. 887 (1927); *Ex parte* Tully, 70 Fla. 1 (1914).

[11] *Ex parte* Perkins, 40 S. W. (2d) 123 (Tex. 1931); *Ex parte* Donohoe, 112 Tex. Cr. App. 124, 14 S. W. (2d) 848 (1929); In re Haigler, 15 Ariz. 150, 137 Pac. 423 (1913); State v. District Court, 35 Mont. 504 (1907); State v. Kaufman, 20 S. D. 620 (1906).

[12] State v. Butler, 40 La. Ann. 3, 3 So. 350 (1888); State v. Kuchler, 120 Atl. 632 (N. J. 1925); State v. Diehl, 115 Ohio St. 454, 154 N. E. 726 (1926).

a rebuttable presumption of that fact;[13] and in four, it is given no weight.[14] In a recent case, the Supreme Court of Kentucky argued that, in view of the rule that the presumption of innocence remains until conviction and that bail is generally granted, the burden of proving evidence of guilt sufficient to warrant a denial of bail should rest upon the state after as well as before indictment.[15] Where the death penalty has been abolished, it has been held that the exception of capital cases from the constitutional guarantee is ineffective and that in all cases bail is mandatory before conviction.[16] However, in jurisdictions in which the death penalty may be inflicted, a case is "capital" within the meaning of statutes denying bail in capital cases after conviction pending appellate review even though a sentence of life imprisonment has been imposed.[17] This distinction seems to result naturally from the general definition of capital cases as those in which the death penalty may be imposed.[18]

It is well established that the general constitutional guarantee of bail is applicable only before conviction,[19] and although the constitutions of eighteen states provide a further guarantee of bail after conviction pending appeal in a variety of cases less than capital,[20] ordinarily the power to admit a convicted prisoner to bail is entrusted to the discretion of the trial court. Frequently statutes provide that bail should not be granted in capital cases after conviction;[21] but if the conviction has been reversed for

[13] Deaver v. State, 135 So. 604 (Ala. 1931); In re Losasso, 15 Colo. 163 (1890); Rigdon v. State, 41 Fla. 308, 26 So. 711 (1899); State v. Hedges, 177 Ind. 589 (1911); *Ex parte* Towndrow, 20 N. M. 631, 151 Pac. 761 (1915); *Ex parte* Fraley, 3 Okl. Cr. 719, 109 Pac. 295 (1910); State v. Crocker, 5 Wyo. 385, 40 Pac. 681 (1895).

[14] Jordan v. State, 25 Ariz. 249, 215 Pac. 926 (1923); Ford v. Dilley, 174 Iowa 243, 156 N. W. 513 (1916); *Ex parte* Verden, 291 Mo. 552, 237 S. W. 734 (1921); *Ex parte* Howard, 99 Tex. Cr. App. 456, 270 S. W. 550 (1925).

[15] Commonwealth v. Stahl, 237 Ky. 388, 35 S. W. (2d) 563 (1931).

[16] *Ex parte* Ball, 106 Kan. 536, 188 Pac. 424 (1920); see In re Welisch, 18 Ariz. 517, 520, 163 Pac. 264, 265 (1917).

[17] People v. St. Lucia, 315 Ill. 258, 146 N. E. 183 (1925); State v. Barone, 96 N. J. L. 374, 114 Atl. 809 (1921); *Ex parte* Herndon, 18 Okl. Cr. 68, 192 Pac. 820 (1920). *Contra:* Walker v. State, 138 Ark. 517, 209 S. W. 86 (1919).

[18] See cases cited *supra* note 17; 1 BOUVIER, LAW DICTIONARY (3d ed. 1914) 419.

[19] See Note (1922) 19 A. L. R. 807, and In re Halsey (Ohio), U. S. Daily, Nov. 17, 1931, at 2114. *Contra:* State v. Williamson, 135 La. 662, 65 So. 877 (1914).

[20] See CODE CRIMINAL PROCEDURE (Am. L. Inst. 1928) 266. In ten states bail is a matter of right when the appeal is from a judgment imposing a fine only. *Ibid.* 264.

[21] ARK. DIG. STAT. (Crawford & Moses, 1921) § 2958; COLO. COMP. LAWS (1921) §7113; DEL. REV. CODE (1915) § 3980; FLA. REV. STAT. (1920) § 6151; IND. ANN. STAT. (Burns, 1926) § 2386; IOWA CODE (1924) § 13610;

insufficient evidence, bail is generally allowed pending retrial on the ground that the reversal indicates that the death penalty will not be inflicted.[22]

If bail is once granted, no review is open to the prosecution.[23] The effectiveness of a magistrate's discretionary ruling, however, is limited by the practice whereby a prisoner whose application for bail has been denied presents successive applications to other magistrates.[24] The evil of peddling bail petitions has been encouraged by the lack of information concerning previous denials of application and by the failure of magistrates to attach sufficient weight to a previous denial. New York has attempted to remedy this condition by enacting a statute requiring an applicant for bail to list, on oath, any previous applications,[25] but it is evident that this provision will be ineffective unless magistrates will regard a previous order denying bail as presumptively correct, in accord with the rule adopted on appellate review of a bail order.[26]

The bail system derives most of its flexibility from the virtually unlimited discretion of magistrates in fixing the amount of bail. It is true that the constitutions of practically all jurisdictions provide that, "Excessive bail shall not be required."[27] But the courts have interpreted this provision in favor of a liberal exercise of discretionary power, and have held bail to be excessive only if the amount required is unnecessary to secure the compliance of the accused with the conditions of the bail bond, and not merely because he cannot obtain it.[28] Furthermore, while

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KY. CODES (Carroll, 1927) Cr. Prac., § 75; S. C. CODE OF LAWS (1922) § 121. In Louisiana the granting of bail after conviction for a capital offense is forbidden by the constitution. Art. I, § 12. See generally Note (1926) 45 A. L. R. 458.

[22] *Ex parte* Westcott, 57 Cal. App. 4, 270 Pac. 247 (1928); *Ex parte* Davis, 28 S. W. (2d) 165 (Tex. 1930). But if competent evidence indicates that the death penalty will be inflicted upon new trial, bail is denied. *Ex parte* Berwick, 33 S. W. (2d) 444 (Tex. 1930); Cofer v. Henderson, 131 So. 421 (Miss. 1930).

[23] See the practice in In re Pantages, 209 Cal. 535, 291 Pac. 831 (1930) and in United States v. Morton, 10 F. (2d) 657 (C. C. A. 7th, 1926). Legislation in four states restricts the number of original applications which may be made. ALA. CODE (1923) § 3368; N. Y. CR. CODE (Gilbert, 1930) § 563; ORE LAWS (Olson, 1920) § 1642; TENN. ANN. CODE (Shannon, 1917) § 7114.

[24] *Ex parte* Marshall, 300 Pac. 1011 (Ariz. 1931).

[25] N. Y. CR. CODE (Gilbert, 1930) § 556-a. See also CODE CRIMINAL PROCEDURE (Am. L. Inst. 1928) § 76.

[26] *Ex parte* Turner, 112 Cal. 627, 45 Pac. 571 (1896); *Ex parte* Rublo, 18 Okl. Cr. 134, 193 Pac. 1009 (1920); State v. Rosander, 46 S. D. 516, 194 N. W. 837 (1923).

[27] N. Y. CONST., art. I, § 5; MASS. CONST., art. II, § 20; CALIF. CONST., art. I, § 6. Illinois has no such provision.

[28] *Ex parte* Malley, 50 Nev. 248, 256 Pac. 512 (1927); *Ex parte* Spoon,

the magistrate allowing bail may at any time require additional security or may revise its amount,[29] an appellate court will reduce the amount fixed only in extreme cases, the rule being that for purposes of an application to reduce the amount of the bail the accused is presumed guilty of the offense charged.[30] Effective exercise of this large discretion presupposes a careful consideration of the character, previous record and financial circumstances of the accused, the nature of the offense charged, and the severity of its penalty, as indicia of the inducement to abscond.[31] The sort of routine administration of bail, however, which actually obtains in so many instances,[32] renders the success of the system largely fortuitous.

Originally a person released on bail was deemed delivered into the personal custody of his sureties, who were generally relatives or friends.[33] This personal relation presumably deterred the accused from forfeiting his bail and inflicting a loss upon his sureties, and further permitted surveillance by the sureties who might at any time surrender the accused into court and secure their own exoneration.[34] In contemporary England bail is still generally required to be furnished by friends or relatives of the accused.[35] But in the United States the widespread operations of surety companies and professional bondsmen have divested the relationship between the accused and his sureties of any personal element,[36] and unquestionably decreased the effectiveness of the obligation. And whatever effectiveness might be left is destroyed by acceptance of worthless sureties and by a notorious failure to enforce forfeitures.[37] In some states legis-

18 Okl. Cr. 703, 192 Pac. 698 (1920); *Ex parte* Glass, 81 W. Va. 111, 93 S. E. 1036 (1917). *Cf.* People v. Snow, 34 Ill. 464, 173 N. E. 8 (1930) ($50,000 bail required of one held on vagrancy charge, but clearly habitual criminal, held unreasonable and reduced to $5,000).

[29] People v. Eiseman, 69 Cal. App. 143, 230 Pac. 669 (1924); In re Mariano, 34 R. I. 534, 84 Atl. 1086 (1912); *Ex parte* Reis, 33 S. W. (2d) 435 (Tex. 1930).

[30] *Ex parte* Grimes, 98 Cal. App. 10, 277 Pac. 1052 (1929); *Ex parte* Horiuchi, 105 Cal. App. 714, 288 Pac. 708 (1930); *Ex parte* Ruble, *supra* note 26.

[31] People v. Searles, 229 App. Div. 603, 243 N. Y. Supp. 15 (3d Dep't 1930); *Ex parte* Bice, 107 Tex. Cr. 87, 296 S. W. 541 (1927).

[32] BEELEY, *op. cit. supra* note 1, at 31, 33, 159. In *Ex parte* Reis, *supra* note 29, the practice of endorsing the amount of bail on indictments presumably without any examination of the accused is revealed.

[33] 4 BL. COMM. *297.

[34] HALE, CROWN PLEAS *124; 1 CHITTY, CRIMINAL LAW *124.

[35] HOWARD, CRIMINAL JUSTICE IN ENGLAND (1931) 339, 340.

[36] BEELEY, *op. cit. supra* note 1, at 39.

[37] Waite, *The Problem of Bail* (1929) 15 A. B. A. J. 71. The results of several crime surveys showing the lax enforcement of bail bond forfeitures are collected and commented upon in WILLOUGHBY, PRINCIPLES OF JUDICIAL ADMINISTRATION (1929) 562 *et seq.*

lation has been enacted prescribing the qualifications of sureties and expediting the enforcement of forfeiture.[38]

Where a person charged with a petty offense is well established in the community and is certain to make no attempt to abscond, it may be desirable that he be relieved of the expense and inconvenience of providing bond. Two methods of securing this end have been suggested: the substitution of a summons for a warrant so that the accused is never committed to confinement pending trial, and the substitution of a personal recognizance for a bond with sureties.[39] While the latter procedure has the advantage of adding a pecuniary sanction to enforce compliance, it may be of doubtful validity in those jurisdictions in which constitutional or statutory provisions prescribe that persons shall be bailable by sufficient sureties,[40] unless, as is possible, the requirement of sureties be held directory only.

The same necessity of securing a person's attendance upon judicial proceedings without subjecting him to confinement has induced almost all jurisdictions to enact statutes permitting or requiring the committing magistrate to cause material witnesses for the prosecution to enter into a recognizance for their appearance to testify.[41] The desirability of such a requirement

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[38] Statutes are collected in 1 CODE OF CRIMINAL PROCEDURE (Am. L. Inst. 1928) 282 *et seq.* See especially, N. Y. CR. CODE (Gilbert, 1930) §§ 569, 593, 595.

[39] Cobb, *Bondsmen Fatten on Needless Bail*, 9 PANEL 39 (1931); BEELEY, *op. cit. supra* note 1, at 154, 155; CRIMINAL JUSTICE IN CLEVELAND (1922) 203. In England, the magistrate may dispense with sureties. ARCHBOLD, CRIMINAL PRACTICE (28th ed. 1931) 90.

[40] *Supra* notes 2 and 4.

[41] *Discretionary:* CAL. PEN. CODE (Deering, 1923) § 878; GA. ANN. CODE (Michie, 1926) PENAL CODE § 940; IDAHO COMP. STAT. (1919) § 8762; MISS. ANN. CODE (1930) § 3007; MONT. REV. CODES (Choate, 1921) § 11791; N. J. COMP. STAT. (1910) 1828, § 25; N. D. COMP. LAWS ANN. (1913) § 10617; OKLA. COMP. STAT. ANN. (1921) § 2503, 3003; ORE. CODE (1930) c. 13, § 2230; PA. STATUTES (Purdon, 1931) c. 19, § 651; R. I. GEN. LAWS (1923) § 6315; S. D. COMP. LAWS (1929) § 4588; TEX. ANN. STAT. (Vernon, 1925) CODE CRIM. PROC. art. 300; UTAH COMP. LAWS (1917) § 8761; VT. GEN. LAWS (1917) § 2557; WYO. COMP. STAT. (1920) § 7359.

Mandatory: ALA. CODE (1928) § 5242; ARK. DIG. STAT. (Crawford & Moses 1921) § 2935; COLO. ANN. STAT. (Mills, 1930) § 3349; DEL. REV. CODE (1915) § 3972; FLA. GEN. LAWS (Skillman, 1927) § 8341; ILL. REV. STAT. (Smith-Howard, 1929) c. 38, § 683; IND. ANN. STAT. (Burns, 1926) § 2110; KAN. REV. STAT. ANN. (1923) c. 62, § 623; KY. CODES (Carroll, 1927) Crim. Prac. Code § 69; ME. REV. STAT. (1930) c. 145, § 16; MASS. GEN. LAWS (1921) c. 276, § 45; MINN. STAT. (Mason, 1927) § 10589; MO. REV. STAT. (1929) § 3483 (if a felony is charged); N. H. PUB. LAWS (1926) c. 366, § 33; N. M. ANN. STAT. (1929) c. 79, § 215; N. C. CODE (1927) § 4568; OHIO CRIM. CODE (Patterson, 1929) § 1433 (15); S. C. CODE CRIM. PRAC. (1922) c. 2, § 16; TENN. ANN. CODE (Shannon, 1919)

was early recognized in English law,[42] and Hale speaks of it as more ordinary and more effectual than the subpoena to secure the attendance of witnesses.[43] However, the efficacy of the system is impaired in some states by limiting the amount at which the recognizance can be fixed to a figure so low as to make it ineffective where there is a strong inducement not to testify,[44] and by lack of statutory authority to require sureties, in which case the magistrate must accept a personal recognizance in all cases.[45] An absolute requirement of sureties may also work an injustice upon a witness who is committed to jail merely because of honest inability to procure sureties.[46] In such a case some statutes provide for the taking of a deposition and the release of the witness upon his own recognizance.[47]

It is evident that the efficiency of a bail system is ultimately dependent upon its administrators. Yet the value of well-considered legislative reforms cannot be minimized.[48] For large cities, where the problem is particularly acute, Detroit's experience with a centralized municipal criminal court indicates that centralization of administration would improve the bail system as well as increase efficiency in other aspects of criminal administration.[49] Centralization would permit a closer scrutiny

§ 7026; W. VA. CODE ANN. (1931) c. 62, art. 3, § 13; WASH. COMP. STAT. (Remington, 1922) § 1959. In Crosby v. Potts, 8 Ga. App. 463, 69 S. E. 582 (1910) it was held that the power exists independently of statute. *Contra:* Little v. Territory, 28 Okla. 1467, 114 Pac. 699 (1911).

[42] 1 & 2 Ph. & Mary, c. 13 (1554) permitted magistrates to require a recognizance of material witnesses.

[43] 2 HALE, CROWN PLEAS *282.

[44] ALA. CODE (1928) § 5242 ($100); IDAHO COMP. STAT. (1919) § 8762 ($500); TENN. ANN. CODE (Shannon, 1919) § 7026 ($250); UTAH COMP. LAWS (1917) § 8761 ($200).

[45] *Ex parte* Shaw, 61 Cal. 58 (1882). Comfort v. Kittle, 81 Iowa 179, 46 N. W. 988 (1890). *Cf.* Little v. Territory, *supra* note 14.

[46] Medalie, *Symposium on Material Witnesses*, 8 PANEL 1 (1930) (sailor jailed as material witness for nine months because of failure to furnish bond). See United States v. Lloyd, 4 Blatchf. 427, Fed. Cas. No. 15, 614 (C. C. S. D. N. Y. 1860).

[47] MASS GEN. LAWS (1921) c. 276, §§ 49, 51; MONT. REV. CODES (Choate, 1921) § 11794; UTAH COMP. LAWS (1921) § 8765; WASH. COMP. STAT. (Remington, 1922) § 1962. If a witness is unable to provide sureties, he shall be released on his own recognizance. TEX. ANN. STAT. (Vernon, 1925) CODE CRIM. PROC., art. 300; MINN. STAT. (Mason, 1927) § 10589 (except in cases of murder, arson involving the loss of life, and criminal abuse of children). In Illinois, a statue expressly provides that no witness shall be compelled to give other security than his own recognizance. ILL. REV. STAT. (Smith-Hurd, 1929) c. 38 § 683.

[48] See generally, CODE OF CRIMINAL PROCEDURE (Am. L. Inst. 1928) §§ 35-56.

[49] Harley, *Detroit's New Model Criminal Court* (1920) 11 J. Crim. L. 389-404.

of bondsmen by confining their operations to a single court; it would tend to restrict the practice of peddling applications for bail; and it would facilitate observation and criticism of bail administration.